DOCKET

No. 07-512

Title: Pacific Bell Telephone Company, dba AT&T California, et al., Petitioners

v.

linkLine Communications, Inc., et al.

Docketed: October 17, 2007

Lower Ct: United States Court of Appeals for the Ninth Circuit

Case Nos.: (05-56023)

Decision Date: September 11, 2007

Questions Presented

~~Date~~~	~~~~~~~~Proceedings and Orders~~~~~~~~~~~~~~~~~~~~~~
Oct 17 2007	Petition for a writ of certiorari filed. (Response due November 16, 2007)
Oct 29 2007	Order extending time to file response to petition to and including December 17, 2007.
Oct 30 2007	Consent to the filing of amicus briefs in support of either party or neither party received from counsel for the petitioners
Nov 15 2007	Brief amici curiae of Verizon Communications Inc., et al. filed.
Nov 16 2007	Brief amici curiae of Profesors and Scholars in Law and Economics filed.
Nov 16 2007	Brief amici curiae of Commonwealth of Virginia and Nine Other States filed.
Dec 17 2007	Brief of respondents LinkLine Communications, Inc., et al. in opposition filed
Dec 28 2007	Reply of petitioners Pacific Bell Telephone Company, dba AT&T California, et al. filed.
Jan 2 2008	DISTRIBUTED for Conference of January 18, 2008.
Jan 22 2008	The Solicitor General is invited to file a brief in this case expressing the views of the United States.
May 22 2008	Brief amicus curiae of United States filed.
May 30 2008	Supplemental brief of respondents LinkLine Communications, Inc., et al. filed.
Jun 3 2008	DISTRIBUTED for Conference of June 19, 2008.
Jun 23 2008	Petition GRANTED.
Jul 3 2008	Consent to the filing of amicus curiae briefs in support of either or neither party received from counsel for the petitioners.
Jul 9 2008	The time within which to file the joint appendix and petitioners' brief on the merits is extended to and including August 28, 2008.
Aug 28 2008	Joint appendix filed. (Statement of costs filed)
Aug 28 2008	Brief of petitioners Pacific Bell Telephone Company, dba AT&T California, et al. filed.

Sep 3 2008	Brief amici curiae of Professors and Scholars in Law and Economics filed.
Sep 4 2008	Brief amicus curiae of United States filed.
Sep 4 2008	Brief amicus curiae of Abbott Laboratories filed.
Sep 4 2008	Brief amici curiae of Verizon Communications Inc., et al. filed.
Sep 4 2008	Brief amici curiae of Commonwealth of Virginia and 8 Other States filed.
Sep 4 2008	Brief amicus curiae of Washington Legal Foundation filed.
Sep 8 2008	SET FOR ARGUMENT ON Monday, December 8, 2008.
Sep 9 2008	Extension of time within which to file respondents' brief on the merits to and including October 14, 2008.
Sep 23 2008	CIRCULATED.
Oct 6 2008	Record received from the U.S.C.A. for the 9th Circuit. (1 envelope)
Oct 9 2008	Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed.
Oct 14 2008	Brief of respondents linkLine Communications, Inc., et al. filed. (Distributed)
Oct 21 2008	Brief amicus curiae of Comptel filed. (Distributed)
Oct 21 2008	Brief amicus curiae of American Antitrust Institute filed. (Distributed)
Oct 22 2008	Motion for leave to file out-of-time and motion of American Antitrust Institute for leave to participate in oral argument as amicus curiae and for divided argument filed.
Oct 28 2008	Record received from the U.S.D.C. for the Central District of California. (1 box)
Oct 29 2008	Letter from counsel for the petitioners addressing motion of American Antitrust Institute for leave to participate in oral argument as amicus curiae and for divided argument.
Nov 13 2008	Reply of petitioners Pacific Bell Telephone Company, dba AT&T California, et al. filed. (Distributed)
Nov 17 2008	Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED.
Nov 17 2008	Motion for leave to participate in oral argument as amicus curiae and for divided argument GRANTED and the time is to be divided as follows: 15 minutes for respondents, and 15 minutes for amicus curiae American Antitrust Institute.
Dec 8 2008	Argued. For petitioners: Aaron Panner, Washington, D.C.; and Deanne E. Maynard, Assistant to the Solicitor General, Department of Justice, Washington, D.C. (for United States, as amicus curiae.) For respondents: Maxwell M. Blecher, Los Angeles, Cal.; and Richard M. Brunell, Newton, Mass. (for American Antitrust Institute, as amicus curiae.)
Dec 16 2008	Letter from counsel for amicus American Antitrust Institute received. (Distributed)

PETITION FOR WRIT OF CERTIORARI

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Supreme Court, U.S.
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IN THE
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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October 17, 2007

QUESTION PRESENTED

Whether a plaintiff states a claim under Section 2 of the Sherman Act by alleging that the defendant – a vertically integrated retail competitor with an alleged monopoly at the wholesale level but no antitrust duty to provide the wholesale input to competitors – engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete.

LIST OF PARTIES TO THE PROCEEDINGS

Petitioners Pacific Bell Telephone Company (which now does business as AT&T California (formerly SBC California)), Pacific Bell Internet Services (now known as SBC Internet Services, Inc. d/b/a AT&T Internet Services and AT&T Entertainment Services), and SBC Advanced Solutions, Inc. (d/b/a AT&T Advanced Solutions) were the defendants in the district court proceedings and the appellants in the court of appeals proceedings.

Respondents linkLine Communications, Inc., In-Reach Internet LLC (now known as InReach Internet, Inc.), Om Networks d/b/a Omsoft Technologies, and Nitelog, Inc. d/b/a Red Shift Internet Services were the plaintiffs in the district court proceedings and appellees in the court of appeals proceedings.

CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 29.6 of the Rules of this Court, petitioners Pacific Bell Telephone Company (which now does business as AT&T California (formerly SBC California)), Pacific Bell Internet Services (now known as SBC Internet Services, Inc. d/b/a AT&T Internet Services and AT&T Entertainment Services), and SBC Advanced Solutions, Inc. (d/b/a AT&T Advanced Solutions) state the following:

Pacific Bell Telephone Company is a wholly owned subsidiary of AT&T Teleholdings, Inc., which is a wholly owned subsidiary of AT&T Inc. (formerly SBC Communications Inc.). AT&T Inc. has no corporate parent. No publicly held corporation owns 10% or more of the stock of AT&T Inc. AT&T California (formerly SBC California) is the trade name under which Pacific Bell Telephone Company does business in California.

SBC Internet Services, Inc. (formerly Pacific Bell Internet Services) is wholly owned by AT&T Teleholdings, Inc., which is wholly owned by AT&T Inc. SBC Internet Services, Inc. does business under the trade names AT&T Internet Services and AT&T Entertainment Services.

SBC Advanced Solutions, Inc. is jointly owned by AT&T Inc. and AT&T Teleholdings, Inc. SBC Advanced Solutions, Inc. does business under the trade name AT&T Advanced Solutions.

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Petitioners Pacific Bell Telephone Company d/b/a AT&T California, Pacific Bell Internet Services (now known as SBC Internet Services, Inc. d/b/a AT&T Internet Services and AT&T Entertainment Services), and SBC Advanced Solutions, Inc. d/b/a AT&T Advanced Solutions respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-24a) will be, but has not yet been, reported (it is available at 2007 WL 2597258). The orders of the district court (Pet. App. 25a-57a, 58a-91a) are not reported.

JURISDICTION

The court of appeals entered its judgment on September 11, 2007. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

Section 2 of the Sherman Act, 15 U.S.C. § 2, provides:

> Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.

INTRODUCTION

Respondents (plaintiffs below) purchase telecommunications services at wholesale from petitioners (collectively, "AT&T") and use them to provide retail Internet-access service in competition with AT&T. They alleged that AT&T was a monopolist at the wholesale level and had violated Section 2 of the Sherman Act by creating a "price squeeze," that is, by leaving insufficient margin between the wholesale and retail prices that AT&T charged. The Ninth Circuit – stating that "price squeeze theory form[s] part of the fabric of traditional antitrust law," Pet. App. 14a – ruled that respondents had stated a claim, even though, as the Ninth Circuit acknowledged, under this Court's decision in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), AT&T – which had not engaged in a relevant prior voluntary course of dealing – had no antitrust duty to offer the wholesale input to competitors. And it did so despite its acknowledgement that the D.C. Circuit had recently ruled, in indistinguishable circumstances, that such a claim could *not* proceed. *See Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673-74 (D.C. Cir. 2005).

The Ninth Circuit has thus decided an important and recurring question of antitrust law in a manner that creates a square circuit-court conflict. The decision also contradicts and undermines *Trinko*, by creating a purported exception to *Trinko*'s rule that – in the absence of any antitrust duty to deal – a rival's allegations that a monopolist has provided insufficient assistance fail to state a claim under Section 2. Moreover, the Ninth Circuit's recognition of price-squeeze claims as an independent basis for liability under Section 2 threatens to harm consumers by

deterring conduct that promotes efficiency and reduces retail prices. Partial vertical integration – the situation where a company both sells an upstream wholesale input to rivals and produces the downstream product itself – is ubiquitous. Under the decision below, any vertically integrated producer with market power at the wholesale level is potentially subject to a claim of "price squeeze" if the combination of its wholesale and resale prices makes competitive life difficult for its rivals. Yet this Court has recognized that Section 2 does not prevent a legitimate monopolist from charging high prices. And low prices are not unlawful unless predatory pursuant to the standard established in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), which requires pricing below cost and a likelihood of recoupment of any losses, neither of which plaintiffs alleged below. The Ninth Circuit's erroneous decision deters voluntary dealing, efficient vertical integration, and retail price competition that benefit consumers.

Last Term, the Court reversed the Ninth Circuit's standard governing predatory bidding claims, after the United States had warned that the decision, if left unreviewed, "threaten[ed] to chill procompetitive conduct by firms in a wide variety of markets." Brief for the United States As Amicus Curiae at 19, *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, No. 05-381 (U.S. filed May 26, 2006). The same concern is emphatically present in this case. This Court should grant certiorari and reverse.

STATEMENT OF THE CASE

1. The District Court's Rulings

Respondents purchase a high-speed digital subscriber line service (known as "DSL transport") from AT&T, combine it with other facilities and services, and then sell retail Internet-access service in competition with AT&T. They sued, claiming that AT&T had engaged in monopolization and attempted monopolization in violation of Section 2 of the Sherman Act by refusing to deal, by denying access to an "essential facility," and by engaging in a "price squeeze." After this Court decided *Trinko*, AT&T moved to dismiss the claims, noting that AT&T had provided DSL transport to rival providers of retail Internet-access service only under compulsion of Federal Communications Commission ("FCC") regulations;[1] that AT&T had no *antitrust* duty to deal with respondents at all; and that respondents' complaints about the terms of dealing between petitioners and respondents therefore failed to state a claim under Section 2. *Cf.* 540 U.S. at 409-10.

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[1] Under the FCC regulations in place during the relevant period, DSL transport – which provides transmission capacity over local telephone lines – was characterized as a basic service (or, in the parlance of the Telecommunications Act of 1996, a telecommunications service) while DSL-based high-speed Internet-access service was characterized as an enhanced service (or information service). *See generally National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 975-77, 992-94 (2005). Under the FCC's "*Computer III*" regime – *see* Report and Order, *Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, 104 F.C.C.2d 958, 964, ¶ 4 (1986) – telephone companies were permitted to provide enhanced services on an integrated basis only if they also offered underlying basic services to rival providers of enhanced services on a nondiscriminatory basis. *See Brand X*, 545 U.S. at 995; *see also* Pet. App. 5a n.6.

The district court agreed that the refusal-to-deal and essential-facilities claims could not proceed. *See* Pet. App. 77a-86a. The court refused to dismiss the price-squeeze claim, however, finding that *Trinko* "simply does not involve price-squeeze claims." *Id.* at 86a. The court also rejected the argument that price-squeeze claims are unavailable when "wholesale prices are regulated by a federal regulatory agency," *id.* at 87a-88a, finding the argument inconsistent with the Ninth Circuit's analysis in *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992).

As ordered by the district court, respondents amended their complaint to elaborate on their price-squeeze claim. The amended complaint alleged that "defendants unlawfully manipulated their dual role" as a "wholesale-monopoly supplier and retail competitor" by "intentionally charging independent [Internet service providers ("ISPs")] wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services . . . thereby making it impossible for independent ISP competitors . . . to compete at the low retail prices set by defendants." Am. Compl. ¶ 25(A)(1) (quoted at Pet. App. 5a-6a).[2]

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[2] The amended complaint further alleged that "for a period" AT&T had "charg[ed] wholesale DSL [transport] prices . . . that actually exceeded the prices at which [AT&T] . . . was charging retail end-user customers." Am. Compl. ¶ 25(A)(1) (quoted at Pet. App. 6a). Respondents alleged that, if they charged the same price for Internet-access service as AT&T, they "could not cover the cost of providing [retail] service," and that, if AT&T "charged [its] retail affiliates the same wholesale costs for DSL transport that they charged their wholesale . . . customers . . . , defendants could not cover their wholesale costs and make a profit." *Id.* ¶ 25(A)(2)-(3) (quoted at Pet. App. 6a).

AT&T again moved to dismiss, arguing that the claim could proceed only if plaintiffs alleged facts supporting the two prerequisites for a predatory-pricing claim under *Brooke Group* – that is, pricing of the retail Internet-access service below cost and a likelihood of recoupment. Although the district court found that there was "persuasive appeal to [petitioners'] argument that the underlying logic of *Trinko*, which is that no inference of anticompetitive intent can be drawn from a refusal to deal where the parties are compelled by law to deal, applies with equal force to price squeeze claims," Pet. App. 55a, it again denied the motion. In the same order, the court granted petitioners' motion to certify its order for appeal. *See id.* at 56a. The Ninth Circuit granted interlocutory review. *See id.* at 92a.

2. The Ninth Circuit's Opinion

The Ninth Circuit affirmed. The court stated that, "[i]n antitrust terms, a price squeeze occurs 'when a vertically integrated company sets its prices or rates at the first (or "upstream") level so high that its customers cannot compete with it in the second-level (or "downstream") market.'" Pet. App. 8a (citation omitted). The court stated that, "[f]or over six decades, federal courts have recognized price squeeze allegations as stating valid claims under the Sherman Act." *Id.* (citing, *inter alia*, *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 437-38 (2d Cir. 1945) ("*Alcoa*")). The court also noted its prior holding that "claims of

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The amended complaint charged that "defendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent" providers of Internet-access service. *Id.* ¶ 25(A)(3) (quoted at Pet. App. 7a).

price squeezing under § 2 are viable against monopolists in regulated industries." *Id.* at 9a (citing *City of Anaheim*).

The Ninth Circuit acknowledged *Trinko*'s holding that "failure by a monopolist to deal with a competitor on certain service terms when that monopolist was under no duty to deal with the plaintiff . . . did not state a claim under § 2 of the Sherman Act." *Id.* at 9a-10a. It stated that *Trinko* thus "raised the question of whether a price squeeze is merely another term of the deal governed by the Supreme Court's analysis in *Trinko*, or whether it is something else." *Id.* at 10a. Asserting that the circuits were already in conflict over the question, *see id.* (comparing *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050 (11th Cir. 2004) (allowing a "price squeezing" claim to proceed), *cert. denied*, 544 U.S. 904 (2005), with *Covad v. Bell Atlantic*, 398 F.3d at 673-74 (rejecting price-squeeze claim in the absence of a duty to deal in the upstream input)),[3] the court concluded that the case before it was controlled by the Ninth Circuit's earlier decision in *City of Anaheim*, which recognized potential price-squeeze claims. The court thereby decided the question in

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[3] In fact, the Ninth Circuit's suggestion that there was an existing circuit split was mistaken. As AT&T had explained to the Ninth Circuit, what the Eleventh Circuit referred to as "price squeezing" was in substance a claim for predatory pricing under the Supreme Court's test in *Brooke Group*. *See Covad v. BellSouth*, 374 F.3d at 1049-52; *see also Covad Communications Co. v. Bell Atlantic Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005) (order on denial of rehearing) (noting that, in *Covad v. BellSouth*, "the complaint alleged the 'basic prerequisites for . . . price predation'") (quoting 374 F.3d at 1049) (alteration in original); *see also infra* p. 13.

direct and acknowledged conflict with the prior decision of the D.C. Circuit.

The Ninth Circuit offered two reasons for its decision. *First*, it stated that "*Trinko* did not involve a price squeezing theory" and that, "[b]ecause a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." Pet. App. 14a *Second*, the court determined that the standard established in *City of Anaheim* was appropriately circumscribed by the requirement that a plaintiff alleging a price squeeze in a regulated industry show "specific intent on the part of the wholesale monopoly holder to 'serve its monopolistic purposes at [retail competitors'] expense.'" *Id.* (quoting *City of Anaheim*, 955 F.2d at 1378) (alteration in original).

The Ninth Circuit also stated that "the existence of regulation does not always eliminate the danger of anticompetitive harm." *Id.* at 15a. "The key, under *Trinko*, is the nature of the regulatory structure at issue." *Id.* The court found itself "confronted with a partially regulated industry": while, "[a]t the wholesale level, there are a series of regulatory mechanisms and regulatory agencies charged with assuring fair play," *id.* at 16a, there is "no comparable regulatory attention paid to the retail DSL market," *id.* at 18a. "It is unclear at this juncture the extent to which linkLine is basing its § 2 price squeezing theory on wholesale pricing, retail pricing, or both. However, since linkLine could prove facts . . . that involve only unregulated behavior at the retail level,"

its claim could not be dismissed on the pleadings. *Id.*[4]

Judge Gould dissented, stating that *Trinko* "takes the issues of wholesale pricing out of the case," such that plaintiffs would have to allege the elements of a predatory-pricing claim with respect to "retail sales of internet connection[s]" to state a claim under Section 2. *Id.* at 20a-21a. Under this standard, the amended complaint failed to state a claim: "plaintiffs . . . did not allege that the seller had the market power to set prices for internet connection[s] in the retail market, that [petitioners'] retail price, contributing to the squeeze, was set below cost, and that losses could later be recouped." *Id.* at 23a.

REASONS FOR GRANTING THE PETITION

The Ninth Circuit's decision stands in acknowledged conflict with the prior decision of the D.C. Circuit, which recognized that it makes no sense to permit a price-squeeze claim when the defendant has no antitrust duty to deal in the upstream input. It conflicts as well with prior decisions of the Fourth, Seventh, and Eleventh Circuits, which dismissed indistinguishable price-squeeze claims. And the decision provides plaintiffs an end-run around this Court's decision in *Trinko*, which established a categorical limitation on a monopolist's obligation to as-

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[4] The Ninth Circuit directed the district court to judge the viability of the claim at summary judgment based on "whether the complained of behavior took place at the regulated wholesale level, the unregulated retail level, or some combination of the two, and to what extent, if any, the responsible agencies have devoted attention to or had involvement in the complained of conduct." Pet. App. 18a.

sist rivals by dealing with them on favorable terms. For those reasons, the Court should grant certiorari.

Review also is warranted because the Ninth Circuit's decision breathes new life into a price-squeeze doctrine that conflicts with important Sherman Act principles articulated by this Court. The Ninth Circuit's decision begins with the proposition that a plaintiff states a "valid claim[] under the Sherman Act" by alleging that "a vertically integrated company set[] its prices or rates at the first (or 'upstream' level so high that its customers cannot compete with it in the second-level (or 'downstream') market." Pet. App. 8a (internal quotation marks omitted). But a standard that makes the legality of pricing conduct turn on the impact on *competitors* – whether such an impact is "intended" or not – is inconsistent with the bedrock principle that antitrust law is intended for the protection of *competition*, not competitors. Because the Ninth Circuit's decision creates a threat of liability and litigation whenever a vertically integrated firm with market power prices aggressively at the downstream level, the decision promises to deter price cuts that benefit consumers. And the decision will likewise distort business decisions concerning vertical integration and voluntary dealing with downstream rivals, all to the detriment of competition. The Court should accept this opportunity to eliminate price squeeze as an independent basis for liability under Section 2.

I. THE DECISION BELOW - WHICH ALLOWS A PRICE-SQUEEZE CLAIM TO PROCEED EVEN WHEN THE DEFENDANT HAS NO DUTY TO DEAL - CONFLICTS WITH PRIOR CIRCUIT PRECEDENT AND WITH *TRINKO*

A. The Ninth Circuit's Rule Conflicts with the Prior Decision of the D.C. Circuit and the Law in Other Circuits

The Ninth Circuit's determination that a price-squeeze claim may proceed under Section 2 despite the absence of any duty to deal in the underlying wholesale input creates a square conflict with the D.C. Circuit and contradicts prior decisions of the Fourth, Seventh, and Eleventh Circuits as well. The Court should grant certiorari, first of all, to resolve the conflict. *See* Sup. Ct. R. 10(a).

1. The Ninth Circuit understood that, under *Trinko*, "the failure by a monopolist to deal with a competitor on certain service terms when that monopolist was under no duty to deal with the plaintiff competitor absent statutory compulsion, did not state a claim under § 2 of the Sherman Act." Pet. App. 9a-10a. But it reasoned that this holding did not resolve "the question of whether a price squeeze is merely another term of the deal governed by . . . *Trinko*, or whether it is something else." *Id.* at 10a. The Court ruled that, because "*Trinko* did not involve a price squeezing theory" and "took great care to explain that in this particular regulatory context, 'claims that satisfy established antitrust standards' are preserved," plaintiffs' price-squeeze claim was not barred. *Id.* at 14a (quoting 540 U.S. at 406).

As the Ninth Circuit acknowledged, that holding squarely conflicts with the D.C. Circuit's decision in

Covad v. Bell Atlantic. *See id.* at 10a (acknowledging D.C. Circuit's holding that price-squeeze claims in this context do not "survive *Trinko*"). In *Covad v. Bell Atlantic*, Covad provided DSL service in competition with Bell Atlantic, using wholesale inputs purchased from Bell Atlantic. *See* 398 F.3d at 670.[5] As respondents did in this case, Covad claimed that Bell Atlantic had "engaged in anticompetitive conduct" by "pursu[ing] an unlawful 'price squeeze.'" *Id.*[6] Relying on the Second Circuit's decision in *Alcoa*, Covad argued that this price squeeze violated the Sherman Act.

The D.C. Circuit rejected the claim. The court noted that Bell Atlantic had no *antitrust* duty to deal with Covad at the wholesale level; rather, Bell Atlantic's "duty to make those loops available at all" was purely a product of "statutory compulsion." *Id.* at 673. The court therefore "affirm[ed] the district court's dismissal of Covad's § 2 claim based upon a price squeeze," reasoning that a complaint about price squeeze is no different from any other complaint about terms of dealing, and thus barred by

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[5] Covad provided DSL transmission capacity – analogous to the DSL transport service that petitioners provided to respondents – and purchased telephone lines from Bell Atlantic. *See Covad v. Bell Atlantic*, 398 F.3d at 670. Thus (coincidentally) the service that respondents here alleged was the wholesale input for purposes of respondents' price-squeeze claim was the downstream product for purposes of Covad's price-squeeze claim.

[6] The key allegations were that "Bell Atlantic . . . offered and re-sold its DSL services [at retail] . . . at a monthly price . . . very close to, and in some cases less than, the monthly cost Bell Atlantic charge[d] Covad and other wholesale customers for unbundled loops." 398 F.3d at 673 (first set of brackets and second ellipsis added).

Trinko. Thus, "as observed in a leading treatise, 'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Id.* at 673-74 (quoting 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c3, at 129-30 (2d ed. 2002)). From the point of view of antitrust law, the monopolist can avoid the potential for any price-squeeze allegation by not supplying the competitor.

2. The decision below also conflicts with prior decisions of the Fourth, Seventh, and Eleventh Circuits. In *Cavalier Telephone, LLC v. Verizon Virginia Inc.*, 330 F.3d 176 (4th Cir. 2003), *cert. denied*, 540 U.S. 1148 (2004), the Fourth Circuit rejected (in a pre-*Trinko* decision) a price-squeeze claim by a retail competitor that purchased wholesale inputs from the defendant. *See id.* at 181, 190; *see also* Areeda & Hovenkamp ¶ 787c3, at 320 n.1 (Supp. 2007). In *Goldwasser v. Ameritech Corp.*, 222 F.3d 390 (7th Cir. 2000), the Seventh Circuit dismissed on the pleadings a claim that the defendant's "wholesale prices . . . prevent[ed] . . . competitors . . . from offering attractive resale prices to consumers." *Id.* at 395. And, in *Covad v. BellSouth*, although the court allowed a "price squeezing" claim to proceed, the Eleventh Circuit "limited the claim to instances that . . . involved predatory pricing – namely, where prices were below cost but these losses were recouped in a subsequent period of monopoly prices." Areeda & Hovenkamp ¶ 787c3, at 321; *see also Covad v. BellSouth*, 374 F.3d at 1052. As the dissent below noted, respondents made no such allegations. *See* Pet. App. 22a, 23a (stating that "the 'price squeeze' contention boils down to a claim of a predatory pricing on sales

. . . in the retail market" and that "plaintiffs . . . did not allege" the requisite elements).

In sum, the very claim that the Ninth Circuit allowed to proceed would have been dismissed in the Fourth, Seventh, Eleventh, and D.C. Circuits. The split of authority is undeniable. Moreover, further development of the issue is unlikely to resolve the split. Whenever possible, plaintiffs seeking to litigate a price-squeeze claim will take advantage of the rule in the Ninth Circuit rather than litigate in courts where, at a minimum, a plaintiff cannot proceed with any price-squeeze claim without establishing that the defendant has an antitrust duty to deal.

B. The Ninth Circuit's Decision Conflicts with *Trinko*

The decision below merits review for the additional reason that it is inconsistent with and threatens to undermine the result in *Trinko*. Sup. Ct. R. 10(c).[7]

1. Respondents' "price squeeze" claim is logically and legally indistinguishable from the *Trinko* plaintiff's refusal-to-deal and "essential facilities" claims, which were based on the allegation that the defendant refused to provide adequate service. As this Court has noted, "[a]ny claim for excessive rates can be couched as a claim for inadequate services and vice versa." *AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 223 (1998). Allowing plaintiffs' claim to proceed on a price-squeeze theory would thus flout the core holding of *Trinko*. If the Ninth Circuit were

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[7] The Ninth Circuit's holding conflicts so sharply with *Trinko* that this Court may wish to consider summary reversal. *See, e.g. Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46 (1990) (per curiam) (summarily reversing antitrust decision that was in clear tension with prior decisions of this Court); *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (per curiam) (same).

right, plaintiffs might circumvent *Trinko* simply by recasting a claim of *inadequate* access to network elements as a claim of *too-costly* access to network elements.

Furthermore, recognition of a price-squeeze claim in circumstances where there is no underlying duty to deal would entail the same ills underlying the Court's antitrust analysis in *Trinko*. By threatening antitrust liability based in part on allegedly high wholesale prices, such claims impinge on "an important element of the free-market system," that is, a legitimate monopolist's "opportunity to charge monopoly prices." 540 U.S. at 407. Allowing such claims to proceed would thus undermine incentives for "innovation and economic growth." *Id.* More generally, forcing a firm to protect its downstream rivals from the possibility of a price squeeze is one way of "[c]ompelling such firms to share the source of their advantage," which may "lessen the incentive for the monopolist, the rival, or both to invest in . . . economically beneficial facilities." *Id.* at 407-08. Further, it will always be difficult for an adjudicator to distinguish a price squeeze resulting from the defendant's superior efficiency from a price squeeze that reflects "too high" wholesale prices – thus giving rise to a significant risk of false positives. *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 24 (1st Cir. 1990) (Breyer, J.); *see Trinko*, 540 U.S. at 412-14. That possibility will raise the litigation risks associated with vigorous price competition, putting upward pressure on *retail* prices. Thus, "[m]istaken inferences and the resulting false condemnations 'are especially costly, because they chill the very conduct the antitrust laws are designed to protect.'" *Trinko*, 540 U.S. at 414 (quoting *Matsushita Elec. Indus. Co.*

v. Zenith Radio Corp., 475 U.S. 574, 594 (1986)). *See also infra* pp. 23-27.

As an institutional matter, *Trinko* holds that antitrust laws eschew imposition of duties that would "require antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill-suited" – or that would "require continuing supervision of a highly detailed decree." 540 U.S. at 408, 415. Yet the Ninth Circuit's rule would have courts and juries supervise prices at not one but *two* levels – the prices for both wholesale inputs and downstream retail services – and ensure that their interaction did not unduly restrict competitors' ability to compete in the retail market. *See* 3A Areeda & Hovenkamp ¶ 767d2, at 132 (price-squeeze doctrine, as articulated in *Alcoa*, "burdens courts with the prohibitive administrative task of administering the monopolist's prices"). Because that task is beyond judicial competence, "[t]he problem should be deemed irremedia[ble] by antitrust law." *Trinko*, 540 U.S. at 415 (alteration in original; internal quotation marks omitted).

2. *Trinko* mandated dismissal of the claims below for the additional reason that any conceivable threat to competition posed by the alleged "price squeeze" could be remedied through regulatory oversight. As this Court observed in *Trinko*, "[a]ntitrust analysis must always be attuned to the particular structure and circumstances of the industry at issue," including "the significance of regulation." 540 U.S. at 411. Petitioners' duty to provide DSL transport service to respondents was purely a function of then-binding FCC regulations, as the Ninth Circuit recognized. *See supra* note 1. Moreover, the FCC has jurisdiction

not merely to require dealing, but also to regulate its terms – including, if justified, by regulating the relationship between wholesale and retail prices. *Cf. FPC v. Conway Corp.*, 426 U.S. 271 (1976).

The Ninth Circuit believed that, because retail prices of Internet access are not regulated, the existence of regulation at the wholesale level did not preclude respondents' claims. The Ninth Circuit's analysis is incorrect. That the FCC has, for many years, affirmatively determined that it should *not* regulate retail prices of Internet access (and, more recently, has deregulated broadband services more generally) reflects an affirmative (and sound) regulatory judgment, and not absence of regulatory oversight.[8] Here, as in *Trinko*, "a regulatory *structure*" exists "to deter and remedy anticompetitive harm" and "the additional benefit to competition provided by antitrust enforcement will tend to be small." 540 U.S. at 412 (emphasis added); *see also Town of Concord*, 915 U.S. at 25. For that reason as well, the Ninth Circuit should have ruled that respondents failed to state a claim under Section 2.

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[8] *See Brand X*, 545 U.S. at 976-77, 993-94 (describing FCC decision not to regulate enhanced services); *see also* Report and Order and Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853 (2005) (abandoning *Computer III* requirements).

II. THE COURT SHOULD REJECT THE "PRICE SQUEEZE" DOCTRINE ARTICULATED IN THE DECISION BELOW

The Ninth Circuit's embrace of "price squeeze" as a basis for antitrust liability under Section 2 warrants review as well because it presents an issue of significant practical impact and doctrinal importance. Under the Ninth Circuit's standard, the touchstone for liability is that a vertically integrated company has set its upstream wholesale prices "so high that its customers cannot compete with it" in the downstream retail market. Pet. App. 8a (internal quotation marks omitted). That follows the rule first established by the Second Circuit in the influential but widely criticized *Alcoa* decision, which imposed liability under Section 2 when a wholesale-level monopolist set its wholesale prices above a "fair price" and its retail prices so low that competitors were unable to make "a living profit." *Alcoa*, 148 F.2d at 437. A similar version of price-squeeze doctrine had been recognized – before *Trinko* – by the Third Circuit,[9] the Seventh Circuit,[10] and the Eighth Circuit.[11] *See also Delaware & Hudson Ry. Co. v. Consolidated Rail Corp.*, 902 F.2d 174, 179-80 (2d Cir. 1990) (recognizing Section 2 claim where defendant allegedly raised price of access to railroad tracks above reasonable level).

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[9] *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 809-10 (3d Cir. 1984).

[10] *City of Mishawaka v. American Elec. Power Co.*, 616 F.2d 976, 985 (7th Cir. 1980).

[11] *City of Kirkwood v. Union Elec. Co.*, 671 F.2d 1173, 1176 n.4, 1178-79 (8th Cir. 1982).

The Ninth Circuit's decision and the other decisions recognizing price squeeze as an independent antitrust tort stand in tension with the First Circuit's decision in *Town of Concord*, in which the court – while having no occasion to resolve the *Alcoa* rule's viability as a general matter – rejected application of the doctrine in the presence of price regulation at the wholesale and retail levels. *See* 915 F.2d at 25. Moreover, price-squeeze doctrine is contrary to important antitrust principles articulated by this Court. Unless corrected by this Court, the doctrine will continue to deter efficient voluntary dealing and price-cutting, harming consumers.

A. Price-Squeeze Doctrine Protects Competitors, Not Competition

As broadly articulated by the Second Circuit in *Alcoa* and by the Ninth Circuit below, price-squeeze doctrine is inconsistent with Supreme Court precedent. *Alcoa* and its progeny imply that a monopolist has a duty to avoid setting its prices in a manner that injures downstream competitors. But the doctrinal focus on the well-being of rivals is fundamentally inconsistent with the principle that the antitrust laws "were enacted for the protection of *competition* not *competitors*." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (internal quotation marks omitted); *see also* Brief for the United States As Amicus Curiae at 11, *Kaiser Aluminum & Chem. Corp. v. Bonjorno*, No. 84-1907 (U.S. filed May 30, 1986) (arguing that *Alcoa* is incorrect for this reason). As Judge Posner has explained, this principle means that antitrust law does not seek to preserve "competition as a process of rivalry" for its own sake but "competition as a means of promoting economic efficiency." *Olympia Equip. Leasing Co. v.*

Western Union Tel. Co., 797 F.2d 370, 375 (7th Cir. 1986).

That a prolonged price squeeze may "drive independent competitors out of business . . . does not mean that a price squeeze is anticompetitive." *Town of Concord*, 915 F.2d at 23. The principal objection to "price squeeze" – that it allows a first-level monopolist to reduce competition at a second level – is of no inherent competitive significance. *See* 3A Areeda & Hovenkamp ¶ 756b, at 11 ("Even when a monopolist at one essential stage 'monopolizes' a second stage, consumer harm cannot be inferred and is difficult to identify."). In most circumstances "there is only one monopoly profit to be gained from the sale of an end-product or service," such that the elimination of a downstream rival would not generally lead to higher prices. *Western Res., Inc. v. Surface Transp. Bd.*, 109 F.3d 782, 787 (D.C. Cir. 1997).

Further, any possible anticompetitive consequences stemming from the elimination of a second-level rival must be balanced against the likelihood that a price squeeze itself reflects desirable efficiencies. As the leading treatise recognizes, the traditional suspicion of "price squeeze" reflects a misplaced concern about vertical integration. *See* 3A Areeda & Hovenkamp ¶ 767c, at 126 ("it is difficult to see any *competitive* significance [of a price squeeze] apart from the consequences of vertical integration itself"). But vertical integration "can produce significant cost reductions" by enabling the integrating firm to achieve both "'[p]roduction' efficiencies" – that is, "savings in the cost of producing or distributing goods" – and "'[t]ransactional' efficiencies" – that is, avoidance of costs associated with dealing with other firms. *Id.* ¶ 757a, at 23. Where this is so, "prices that squeeze

the less efficient second-level competitors, even to the point of forcing them from the business, could (by lowering costs) lower prices, or, in any event, save economic resources." *Town of Concord*, 915 F.2d at 24. Moreover, when second-level rivals "exhibit[] some market power," a price squeeze may reflect elimination of supracompetitive margins at the second level. 3A Areeda & Hovenkamp ¶ 756b3, at 14-15. In this situation as well, "price will ordinarily come down and output will ordinarily increase." *Id.*; *see Town of Concord*, 915 F.2d at 24-25.

Recognizing that "extension" of a monopoly is not *generally* anticompetitive, this Court has held that Section 2 does not condemn "monopoly leveraging" – use of monopoly power to gain an advantage in a second market – in the absence of anticompetitive conduct. *Trinko*, 540 U.S. at 415 n.4. The pricing behavior at issue in an alleged price squeeze is not anticompetitive conduct. *First*, Section 2 does not prohibit the charging of "high" prices for a monopoly product. "The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system" because it "attracts 'business acumen'" and "induces risk taking that produces innovation and economic growth." *Id.* at 407.

Second, a defendant cannot be held liable for charging "low" but above-cost prices for a downstream product. "[P]rice competition" – in the absence of predatory pricing – "is not predatory activity." *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 118 (1986); *see United States v. Microsoft Corp.*, 253 F.3d 34, 68 (D.C. Cir. 2001) (per curiam). An integrated retail provider could "squeeze" rivals by lowering its prices below its costs, but, where that

is an antitrust wrong, the rules of predatory pricing – which require a plaintiff to show both below-cost pricing and a likelihood of recoupment of losses, *see Brooke Group*, 509 U.S. at 222, 224 – fully address that behavior. *See* 3A Areeda & Hovenkamp ¶ 767c, at 127 (only potential competitive harm from "price squeeze" should be "resolved under the law of predatory pricing").

Any suggestion that a vertically integrated producer must treat the price charged to others for a wholesale input as the cost of the input to itself ignores economic reality and would deprive the producer and consumers of the benefits of vertical integration. *See id.* ¶ 757a, at 24 ("It is not antitrust's purpose to condemn cost-reducing innovations or structures, even if one consequence is to injure rivals unable to match the cost reductions."). As a lawful monopolist in the wholesale product, an integrated producer is entitled to charge its customers the monopoly price for the wholesale input, but it is equally entitled to ignore the price charged to others and instead to consider the *cost* of producing that input in setting its own retail price. *Cf.* Brief for the United States As Amicus Curiae at 15, *Consolidated Rail Corp. v. Delaware & Hudson Ry. Co.*, No. 90-380 (U.S. filed Apr. 5, 1991) (noting that "the implication of [the Second Circuit's] holding is that a monopolist must deal on terms that provide its rival with a reasonable profit" and stating that "such a requirement would be both unsound in theory and unworkable in practice").

B. Continued Recognition of Price Squeeze as a Potential Basis for Liability Harms Consumers

1. The foregoing shows why it is "extremely hard to identify" circumstances where an alleged "price squeeze" reflects anything other than a legitimate effort to achieve efficient vertical integration by a lawful monopolist. 3A Areeda & Hovenkamp ¶ 767c5, at 129. The Ninth Circuit's approach – which treats the *existence* of a price squeeze as sufficient to state a claim under Section 2 – is therefore unjustified as a matter of antitrust policy. Worse, the court's decision will tend to deter conduct that enhances efficiency and that antitrust law should be careful to protect.[12]

First, subjecting a wholesale monopolist to potential liability for a price squeeze would deter efficient vertical integration and socially desirable, voluntary dealing. A monopolist might offer an upstream product, used by producers of two downstream products. If the monopolist begins to produce one of those products itself, it might face the prospect of price-squeeze litigation brought by rival downstream producers. Such a possibility might either deter the monopolist from entering the downstream market (even in cases where it would be more efficient than

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[12] Almost by definition, price-squeeze claims are brought by rivals, not by consumers; consumers benefit from the very downstream prices that discomfit rivals. This provides an additional reason to eliminate such claims. *See* William J. Baumol & Alan S. Blinder, *Economics: Principles & Policy* 275 (10th ed. 2006) (noting that "[o]ne problem that haunts most antitrust litigation is that vigorous competition may look very similar to acts that *undermine* competition and support monopoly power" and that "effective competition by a firm is always tough on its rivals").

existing rivals) or deter the monopolist from selling to downstream producers in the first place. *Cf. Olympia*, 797 F.2d at 375 (if a firm's voluntary dealing with rivals "lay[s] itself open to an antitrust suit," it will likely refrain from such dealing). In either case, consumers are harmed.

Second, the very incidents of vertical integration that yield the greatest consumer benefit – lower-cost production in downstream markets – are precisely those that will "squeeze" downstream competitors. As the Court has remarked with respect to claims of above-cost predatory pricing claims, in many cases, "the exclusionary effect [here, of price squeeze] . . . reflects the lower cost structure of the alleged predator, and so represents competition on the merits." *Brooke Group*, 509 U.S. at 223. A rule that outlaws price squeezes penalizes those instances of vertical integration – and behavior by vertically integrated monopolists – that promise the greatest benefit.

2. The anticompetitive consequences of the Ninth Circuit's price-squeeze standard are aggravated both because the standard is vague and because it purports to govern prices – "the 'central nervous system of the economy.'" *National Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 692 (1978) (quoting *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 226 n.59 (1940)).

a. The *Alcoa* price-squeeze test invoked by the Ninth Circuit – which makes liability turn on a monopolist's "charg[ing] more than a 'fair price' for the primary product while simultaneously charging so little for the secondary product that its second-level competitors cannot make a 'living profit'" – is famously difficult to administer. *Town of Concord*, 915 F.2d at 25.

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" . . . And how should the court respond when costs or demands change over time, as they inevitably will?

Id.

The Ninth Circuit's emphasis on a defendant's "specific intent," Pet. App. 14a (citing *City of Anaheim*, 955 F.2d at 1378), does not help. The intent to gain more business almost always means doing so at the expense of one's rivals. Price cuts thus may bring the greatest benefits when they are intended to exclude downstream competitors. More important, this Court has made clear that, if conduct is not objectively anticompetitive, the fact that it was motivated by hostility to competitors is immaterial. *See Brooke Group*, 509 U.S. at 225.[13]

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[13] While it has been argued that a price-squeeze claim should be treated in some circumstances as a "constructive refusal to deal," Einer Elhauge & Damien Geradin, *Global Antitrust Law and Economics* 458 (2007), there is no reason to believe that the law of unlawful refusals to deal is not fully capable of dealing with any such concern. And, in any event, such a rationale has no application in this case, where, as the Ninth Circuit found (and as *Trinko* makes clear), petitioners had no antitrust duty to deal in the underlying wholesale input.

b. The urgency of addressing the Ninth Circuit's error is heightened by the fact that its rule distorts pricing decisions, exerting upward pressure on the prices that consumers pay. As then-Judge Breyer noted in similar circumstances, "we ask ourselves what advice a lawyer, faced with the [Ninth Circuit's] rule, would have to give a [vertically integrated] client firm considering procompetitive [price-cuts] in a concentrated industry." *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 235 (1st Cir. 1983). Lawyers will have to warn clients that, if such a price-cut would "squeeze" customers that are also downstream competitors, litigation is a likelihood. That threat alone will be sufficient to deter some price cuts: "[I]t is not always necessary to win cases in order to blunt a rival's competitive weapons. Harassment by lawsuit or even the threat of harassment can be a marvelous stimulus to timidity on the part of competitors." William J. Baumol & Janusz A. Ordover, *Use of Antitrust To Subvert Competition*, 28 J.L. & Econ. 247, 254 (1985).

For this reason, this Court has adopted for predatory-pricing claims a rule that is clear and administrable. That rule exempts from antitrust challenge a category of conduct – "above-cost predatory pricing schemes" – that might, as a theoretical matter, harm competition. *See Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1074-75 (2007); *Barry Wright*, 724 F.2d at 233-34. The basic characteristic of a price-squeeze claim – pricing pressure on a downstream rival – has a strongly pro-competitive tendency. The concern that the Ninth Circuit's decision "could, perversely, 'chil[l] legitimate price cutting,' which directly benefits consumers," *Weyerhaeuser*, 127 S. Ct. at 1074 (alteration

in original), further counsels in favor of this Court's repudiation of any standard that subjects price squeezes to Section 2 scrutiny.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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October 17, 2007

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UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 05-56023

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs-Appellees,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants-Appellants.

Appeal from the United States District Court
for the Central District of California
Steven V. Wilson, District Judge, Presiding
D.C. No. CV-03-05265-SVW

Argued and Submitted June 5, 2007
Filed September 11, 2007

Before SIDNEY R. THOMAS, KIM McLANE WARDLAW, and RONALD M. GOULD, Circuit Judges.

THOMAS, Circuit Judge:

This appeal presents the question of whether the Supreme Court's decision in *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) ("*Trinko*"), bars a plaintiff from claiming a violation of § 2 of the Sherman Antitrust Act by virtue of an alleged price squeeze perpetrated by a competitor who also serves as the plaintiff's supplier at the wholesale level, but who has no duty to deal with the plaintiff absent statutory compulsion.

We conclude that it does not, and affirm the order of the district court denying judgment on the pleadings.

I

This action was filed by linkLine Communications, Inc., In-Reach Internet LLC, Om Networks, and Nitelog, Inc. (collectively "linkLine"), who are Internet Service Providers ("ISPs") who sell DSL[1] access to the internet to retail customers.[2] While some ISPs affiliated with local telephone companies own their own infrastructure and facilities for transmitting data between the internet and consumers, these four lease those facilities variously from SBC California, Inc., Pacific Bell Internet Services, and SBC Advanced Solutions, Inc. (collectively "SBC Entities").

As is true in many regions, because of the development of the telecommunications industry and the costs of building the necessary infrastructure, regional monopolies have developed that own and control the lines necessary for the delivery of telecommunication services.[3] These regional telephone

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[1] DSL (digital subscriber line) is one of three popular ways for consumers to connect to the internet. The other two ways are dial-up service and cable modem service. Both DSL and dial-up service use existing phone lines to connect users to the internet, while cable uses the same cable lines used to transmit cable television signals.

[2] For the purposes of this appeal, we assume as true the facts pleaded in linkLine's amended complaint. *See* Fed.R.Civ.P. 12(c).

[3] The story of how these regional monopolies evolved out of the nationwide monopoly held for decades by American Telephone and Telegraph (AT & T) has been told many times. *See, e.g.*, Joseph D. Kearney, *From the Fall of the Bell System to the Telecommunications Act: Regulation of Telecommunications Under Judge Green*, 50 Hastings L.J. 1395, 1403-18 (1999). However, this history is collateral to our review.

companies are known as incumbent local exchange carriers ("ILECs"). ILECs tend to own the local telephone network as well as the telephone lines – known as the "last-mile" – that connect each individual consumer to the network. Because any company seeking to connect with users at the end of these last mile connections must interconnect with the ILEC, the ILEC's facilities are commonly referred to as "bottleneck" facilities.

At the time of the filing of linkLine's amended complaint, the relevant ILEC in this case was SBC California, Inc. ("SBC"), then a subsidiary of SBC Communications.[4] At the time of the filing of the amended complaint Pacific Bell Internet Services ("PBIS") was a subsidiary of SBC which sold DSL internet access to retail consumers using SBC's telephone lines. In June 2000, SBC transferred responsibility for the provisioning and billing of DSL facilities to SBC Advanced Solutions, Inc. ("SBC-ASI"), an affiliate of SBC's and a subsidiary of SBC Communications. The SBC Entities were thus organized so that they sold both wholesale DSL access ("DSL transport services") to independent ISPs as well as retail DSL access (through PBIS and then SBC-ASI) to individual consumers. At the time the amended complaint was filed, the SBC Entities were both a supplier to the Plaintiffs at the wholesale level, and a competitor at the retail level.

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[4] Subsequent to the filing of the instant action, through a series of mergers and acquisitions, the SBC Entities have reorganized. Regulatory considerations we will discuss later in this opinion likely drove the changing structures. However, in this opinion we analyze the facts through the lens of linkLine's complaint.

Linkline filed its original complaint on July 24, 2003, alleging that the SBC Entities, acting as a single entity, have monopolized and attempted to monopolize the regional DSL market in violation of § 2 of the Sherman Act.[5] In support of the § 2 claim, the complaint alleged that SBC Entities:

> (a) created a price squeeze by charging ISP a high wholesale price in relation to the price at which defendants were providing retail services;
>
> (b) intentionally adopted anticompetitive procedures and processes for handling customer ordering and installation to ISPs that are calculated to (i) cause ISP customer disruption and interruption in service, and (ii) create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to defendants;
>
> (c) purposefully created and imposed procedures that impeded, and/or caused significant delays and costs for, end user customers of defendant switching to the services of independent ISPs, including plaintiffs;
>
> (d) misled, harassed and exhibited hostility toward customers of ISPs, including plaintiffs;
>
> (e) disparaged and created doubts about the efficacy and legality of ISPs, including plaintiffs; and
>
> (f) purposefully failed to bill properly for DSL services.

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[5] The complaint also alleged two state law claims that are not relevant to this appeal.

In short, defendants adopted procedures carefully calculated to deny ISPs access to an essential facility and to preserve and maintain its monopoly control of DSL access to the Internet.

On July 6, 2004, the SBC Entities filed a motion for judgment on the pleadings. The district court read linkLine's complaint as alleging three different categories of anticompetitive conduct: refusal to deal, denial of access to an essential facility, and price squeezing. In an order dated October 20, 2004, the district court dismissed the first two as barred by the Supreme Court's decision in *Trinko*.[6] With respect to the price squeezing claim, it ordered the Plaintiffs to file an amended complaint "limited to the price squeeze claim that details beyond the normal requirements of Rule 8 specific facts supporting Plaintiffs' price-squeeze claim." The first amended complaint described the allegation as follows:

> (1) As set forth above defendants unlawfully manipulated their dual role as vertically integrated monopolists as both a wholesale-

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[6] As a predicate to so finding, the district court had to resolve a dispute between the parties as to whether their dealings had been voluntary or required by law. The district court determined that the Defendants were obligated by law to offer their DSL transport facilities to the Plaintiffs under the 1934 Telecommunications Act ("1934 Act") and the FCC rules implementing it. The 1934 Act, as amended, requires that Defendants provide Plaintiffs with access to their DSL transport services on a nondiscriminatory basis, *see In the Matter of Review of Regulatory Requirements for Incumbent LEC Broadband Telecomm. Servs.*, 17 F.C.C.R. 27000, ¶ 18 (2002), and that "[a]ll charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable . . . ." 47 U.S.C. § 201(b). This determination is not disputed on appeal.

monopoly supplier and retail competitor of plaintiffs for DSL by engaging in an unlawful price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services and necessary equipment to end-user customers – and for a period by charging wholesale DSL prices to competing ISPs (such as plaintiffs) that actually exceeded the prices at which defendants retail affiliate (PBI) was charging retail end-user customers for DSL services and necessary equipment – thereby making it impossible for independent ISP competitors such as plaintiffs to compete at the low retail prices set by defendants for combined DSL-Internet Service and necessary equipment provided to end-user customers.

(2) If plaintiffs charged retail DSL-Internet access customers the same retail price as defendants' retail affiliate charged, plaintiffs could not cover the cost of providing DSL service, which costs necessarily includes the wholesale transport costs charged by defendants.

(3) By the same token, if defendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as plaintiffs), defendants could not cover their wholesale costs and make a profit from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation), that were in some cases, and for some

> period, even below the wholesale DSL transport cost. Given the price margin relationship between retail and wholesale prices, defendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as plaintiffs that are both wholesale customers and retail rivals.

In addition, the amended complaint also alleged that the Defendants

> (1) intentionally adopted anticompetitive procedures and processes for handling customer ordering and installation to ISPs that are calculated to (i) cause ISP customer disruption and interruption in service, and (ii) create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to defendants;
>
> (2) purposefully created and imposed procedures that impeded, and/or caused significant delays and costs for, end user customers of defendant switching to the services of independent ISPs, including plaintiffs, and imposed unreasonable and anticompetitive costs of DSL aggregation-backhaul circuits necessary for providing DSL service and particularly given the delays in processing orders, unfairly raised the per-customer costs of independent ISPs trying to compete with defendants.
>
> (3) misled, harassed and exhibited hostility toward customers of ISPs, including plaintiffs;

(4) disparaged and created doubts about the efficacy and legality of ISPs, including plaintiffs; and

(5) purposefully failed to bill properly for DSL services.

In response, the SBC Entities filed various motions challenging the price squeeze allegations and other portions of the amended complaint.

The district court granted in part the relief requested, but denied the motion to dismiss for failure to state a claim. Acting on the request of the SBC Entities, the district court certified the order for interlocutory appeal.

We granted permission to appeal pursuant to 28 U.S.C. § 1292. We review the denial of a motion for judgment on the pleadings de novo. *Doe v. United States*, 419 F.3d 1058, 1061 (9th Cir.2005).

II

In antitrust terms, a price squeeze occurs "when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market." Von Kalinowski et al., 2 *Antitrust Laws and Trade Regulation* § 27.04[1], 27-40 (2d Ed. Matthew Bender 2007). For over six decades, federal courts have recognized price squeeze allegations as stating valid claims under the Sherman Act.[7] *See United States v. Aluminum Co. of Am.*, 148

[7] Section 2 states that "[e]very person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or,

F.2d 416, 437-38 (2d Cir.1945) ("*ALCOA*") (holding price squeeze unlawful); *see also Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 809-11 (3d Cir.1984) (price squeeze is only an antitrust violation if plaintiffs can show that "the defendants deliberately produced the effect" to "destroy its competition"); *Borough of Landsdale v. Philadelphia Elec. Co.*, 692 F.2d 307, 309-10 (3d Cir.1982); *City of Kirkwood v. Union Elec. Co.*, 671 F.2d 1173, 1178-79 (8th Cir.1982) (antitrust liability can still lie for price squeezes even when rates are *regulated*); *City of Groton v. Conn. Light & Power Co.*, 662 F.2d 921 (2d Cir.1981); *City of Mishawaka v. Am. Elec. Power Co.*, 616 F.2d 976, 983-85 (7th Cir.1980) (antitrust liability can lie for price squeezes in regulated industry upon a showing of specific anticompetitive intent).

We have joined our sister circuits in holding that claims of price squeezing under § 2 are viable against monopolists in regulated industries. *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (1992). In *Anaheim*, we held that even in a business where prices were regulated at both the wholesale and the retail level, it was possible for a price squeeze to occur. *Id.* at 1377 ("[I]t is possible for a utility to manipulate its filings and requests in a manner that causes a, at least temporary, squeeze which might be just as effective as one perpetrated by an unregulated actor.").

In *Trinko*, however, the Supreme Court held that the failure by a monopolist to deal with a competitor on certain service terms when that monopolist was

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if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court."

under no duty to deal with the plaintiff competitor absent statutory compulsion, did not state a claim under § 2 of the Sherman Act. This holding raised the question of whether a price squeeze is merely another term of the deal governed by the Supreme Court's analysis in *Trinko*, or whether it is something else. The D.C. and Eleventh Circuits have offered conflicting answers to that question. *Compare Covad Communications Co. v. Bellsouth Corp.*, 374 F.3d 1044, 1050 (11th Cir.2004) ("*Bellsouth*") (holding that price squeeze claims survive *Trinko*), *with Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673 (D.C.Cir.2005) ("*Bell Atlantic*") (holding that they do not).

In *Trinko*, a customer of one of Verizon's rivals sued Verizon Communications, Inc., alleging that Verizon had engaged in anticompetitive practices by discriminatorily delaying orders placed by customers of Verizon's competitors – orders Verizon was required to fill by the Telecommunications Act of 1996.[8] 540 U.S. at 404. Trinko alleged that by rendering poor performance on orders placed through Verizon's competitors, it would sour those customers' relationships with their CLECs and drive them back to

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[8] The Telecommunications Act of 1996 ("1996 Act") established a requirement that ILECs provide access to their networks to competitors in the telecommunication services market (who became known as competitive local exchange carriers, or "CLECs"). 47 U.S.C. § 251(c). ILECs must offer CLECs access to each of their network elements on an "unbundled" or individual basis. *Id.* ILECs must provide these unbundled network elements ("UNEs") "on rates, terms, and conditions that are just, reasonable, and nondiscriminatory. . . ." *Id.* As part of this regulatory regime, ILECs such as Verizon are required to service their competitor's customers when Verizon controls the infrastructure necessary to provide the services at issue.

Verizon. *Id.* Trinko sued Verizon after both the Federal Communications Commission ("FCC") and New York's Public Services Commission ("NYPSC") had already investigated the matter, resulting in a series of orders by the NYPSC and a consent decree with the FCC.

The Supreme Court held that "Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents." *Id.* at 410. *Trinko* began from the premise that the Telecommunications Act of 1996 neither added to nor subtracted from the class of punishable conduct under traditional antitrust laws. *Id.* at 406 (quoting 47 U.S.C. § 152, note ("nothing in [the 1996 Act] shall be construed to modify, impair, or supersede the applicability of any of the antitrust laws")). Accordingly, the Court set out to determine whether Trinko's allegations made out an actionable antitrust claim under the Court's existing refusal-to-deal precedents, irrespective of Verizon's statutory requirements under the 1996 Act.

The Court reiterated that "the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal,'" *id.* at 408 (quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)), but that "the right to refuse to deal with other firms does not mean that the right is unqualified," *id.* (quoting *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 601 (1985)). The Court then stated that it is "very cautious" when recognizing exceptions to the right of refusing to deal and that *Aspen Skiing* was "at or near the outer

boundary of § 2 liability" for refusing to deal. *Id.* at 408-09.[9] In *Aspen Skiing*, the Court saw strong evidence that the defendant's sole purpose in refusing to deal was to attempt to monopolize, "not by competitive zeal but by anticompetitive malice." *Id.* at 409. That evidence included that (1) the parties had "voluntarily engaged in a course of dealing" (proving that the defendant would have done so absent statutory compulsion); (2) the defendant refused even to sell highlands ski passes at retail rates; and (3) the services it was withholding were "otherwise marketed or available to the public." *Id.* at 409-10. Having found no similar evidence in *Trinko*, the Court held that Verizon's alleged insufficient service failed to state a valid antitrust claim since Verizon's refusal to deal with its competitors at all could not even be seen as anticompetitive. *Id.* at 410.

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[9] *Aspen Skiing* involved a claim by the owner of one of the four ski mountains in Aspen, known as Highlands, that the single owner of the other three ski mountains was violating antitrust laws by refusing to sell Highlands passes to its mountains to prevent Highlands from being able to offer consumers a four-mountain multi-pack. 472 U.S. at 595. The two companies had for years prior acted in partnership to offer skiers a four-mountain multi-pack until the owner of the three mountains realized it could freeze out the independently-owned fourth mountain by forcing consumers to choose between a discounted, week-long pass for its three mountains or higher priced individual daily tickets that would permit the consumer to ski all four mountains. The plan worked, and when the owner of the three mountains prevented any attempt by Highlands to sell four-mountain multi-packs (by, among other things, even refusing to sell Highlands passes to its mountains at retail rates), skiers forsook Highlands in favor of the three mountain package. The Court held the owner of the three mountains liable under the antitrust laws.

The Court went on to reason that not only did Trinko's allegations not make out a traditional antitrust claim, but that it would not be justified in extending antitrust liability to include Trinko's case. In reaching this conclusion, it emphasized "the existence of a regulatory structure designed to deter and remedy anticompetitive harm," and the dangers of judicial intervention. *Id.* at 412-14. The latter include the risk of "false condemnations" that might "chill the very conduct the antitrust laws are designed to protect." *Id.* at 414 (quoting *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986)). Importantly, the Court did not say that the existence of a regulatory scheme was a per se bar to judicial enforcement of the antitrust laws, only that "the existence of a regulatory structure" is "*[o]ne factor* of particular importance." *Id.* at 412 (emphasis added). *Trinko* never addressed price squeeze claims specifically. However, *Trinko* is of significant import. Indeed, we have already had occasion to apply *Trinko* to bar antitrust liability when the complaint centered on allegedly anticompetitive price terms, albeit not price squeezes. *See MetroNet Servs Corp. v. Qwest Corp.*, 383 F.3d 1124 (9th Cir.2004).

Given this background, we must decide whether *Trinko* entitles the SBC Entities to judgment on the pleadings, which in turn requires us to decide whether *Anaheim* remains viable after *Trinko*. Normally, only our court, sitting en banc, may overrule our precedent absent an intervening Supreme Court decision or act of Congress. *Cerrato v. San Francisco Cmty. Coll. Dist.*, 26 F.3d 968, 972 n. 15 (9th Cir. 1994). However, "where the reasoning or theory of our prior circuit authority is clearly irreconcilable

with the reasoning or theory of intervening higher authority, a three-judge panel should consider itself bound by the later and controlling authority, and should reject the prior circuit opinion as having been effectively overruled." *Miller v. Gammie*, 335 F.3d 889, 893 (9th Cir.2003) (en banc).

Here, reconsideration of *Anaheim* is not required because the reasoning and theory of *Anaheim* is not "clearly irreconcilable with the reasoning or theory" of *Trinko*. First, as the Eleventh Circuit has underscored, *Trinko* did not involve a price squeezing theory. Indeed, *Trinko* took great care to explain that in this particular regulatory context, "claims that satisfy established antitrust standards" are preserved. 540 U.S. at 406 (citation omitted). Because a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*. *See Bellsouth*, 374 F.3d at 1050 ("price squeezing claim survives [*Trinko*] because it is based on traditional antitrust doctrine").

Second, *Anaheim* did not embrace an unlimited view of § 2 price squeeze liability in regulated industries. To the contrary, *Anaheim* rejected the idea that, in the case of regulated industries, "a mere showing that a price squeeze developed would suffice to cause antitrust liability." 955 F.2d 1378. *Anaheim* recognized that "courts should tread carefully" in imposing antitrust standards on regulated industries, *id.* at 1378, and ultimately required a showing of specific intent on the part of the wholesale monopoly holder to "serve its monopolistic purposes at [retail competitors'] expense" in order for § 2

liability to attach. *Id.* Thus, *Anaheim* recognized the viability of the theory, but carefully circumscribed it.

Trinko did not, as the SBC Entities would argue, completely eliminate the viability of a § 2 price squeeze theory in regulated industries. Were that the case, *Trinko* would not have referred to the existence of a regulatory regime as only "one factor" to consider in determining whether antitrust liability might also lie. 540 U.S. at 412 Moreover, the existence of regulation does not always eliminate the danger of anticompetitive harm. *See Mishawaka*, 616 F.2d at 983-84 (noting that the presence of a regulatory structure offers price squeezers a "ready made illegal opportunity with a legitimate gloss"). The key, under *Trinko*, is the nature of the regulatory structure at issue. As Justice Scalia observed:

> One factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm. Where such a structure exists, the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny. Where, by contrast, "[t]here is nothing built into the regulatory scheme which performances the antitrust function," *Silver v. New York Stock Exchange*, 373 U.S. 341, 358 (1963), the benefits of antitrust are worth its sometimes considerable disadvantages.

Thus, consistent with *Trinko*, 540 U.S. at 412, *Anaheim* rejected the wholesale importation of antitrust theory as applicable to regulated industries. In the particular industry at hand, *Anaheim* recognized that, even in the regulatory scheme at issue, "it is

possible for a utility to manipulate its filings and requests in a manner that causes a, at least temporary, squeeze which might be just as effective as one perpetrated by an unregulated actor." 955 F.2d at 1377. Thus, *Anaheim* undertook a *Trinko*-type analysis in the context of the particular industry and factual setting. Significantly, after examining the particular pleadings, the *Anaheim* panel concluded that the price squeeze theory was not viable in that case. Of course, in any future application of *Anaheim*, we will have to ensure consistency with *Trinko*. However, a careful reading of *Anaheim* does not demonstrate that the holding is "clearly irreconcilable with the reasoning or theory" of *Trinko*.

When we apply *Anaheim* and *Trinko* to this case, the soundness of the district court's conclusion in denying judgment on the pleadings is clear. Here, unlike the circumstances in *Anaheim* and *Trinko*, we are confronted with a partially regulated industry. At the wholesale level, there are a series of regulatory mechanisms and regulatory agencies charged with assuring fair play. These regulations grew out of the 1934 Act and have been considered in a series of FCC decisions known as the "Computer Inquiries."[10] In short, under FCC rules in place at the time of the filing of the complaint, the SBC Entities were subject to certain regulatory requirements if they wished to enter the enhanced services telecommunications market (i.e., offer DSL internet access).

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[10] For a comprehensive explanation of how the regulatory structure operates, see Robert Cannon, *Where Internet Service Providers and Telephone Companies Compete: A Guide to the Computer Inquiries, Enhanced Service Providers and Information Service Providers*, 9 Comm. Law Conspectus 49 (2001) [hereinafter "Guide to the Computer Inquiries"].

If an ILEC wished to offer DSL internet access, it could choose one of two routes. It could form a separate subsidiary through which it would offer DSL internet access, but which had to obtain the infrastructure necessary to provision such services from the ILEC on the same terms as unaffiliated ISPs. *See* 47 C.F.R. § 64.702(c) (codifying the second "Computer Inquiry"). Alternatively, an ILEC could provide DSL internet access itself, but to do so it must file what is known as a "Comparably Efficient Interconnection" plan ("CEI") with the FCC. *See In re Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services, Report and Order*, 14 FCC Rcd. 4289 (1999) [hereinafter "Computer III" order]. These plans indicated how ILECs planned on providing competing ISPs with equal access to all the elements necessary to provide their own DSL internet access services. Among the requirements for CEI plans, ILECs had to "provide competitors with interconnection facilities that minimize transport costs. This provision ensures that [ILECs] cannot require competitive ISPs to purchase unnecessarily expensive methods of interconnection with the [ILECs] network." *Id.*[11] The Act also required that "[a]ll charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable. . . ." 47 U.S.C. § 201(b).

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[11] Under an intervening FCC decision, incumbent LECs are no longer required to allow their competitors to interconnect. *See In re Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 36 Comm. Reg. (P & F) 944, 2005 WL 2347773 (Sept. 25, 2005). This change, however, does not apply to the instant suit and the details of the rationale supporting the change are beyond the scope of this opinion.

The 1934 Act charged the FCC with enforcing these regulations and, in some cases, parties can also bring complaints before state public utility commissions. Aggrieved parties can either file a complaint in federal district court or before the Commission. 47 U.S.C. § 207. The FCC may also initiate its own enforcement proceedings and craft remedies as it deems appropriate. 47 U.S.C. § 205. In practice, however, the FCC tends to rely on market players bringing complaints to its attention. *See* Cannon, *Guide to the Computer Inquires* at 70.

All of this regulation, however, applies only to the wholesale prices the SBC Entities charged linkLine; there is no comparable regulatory attention paid to the retail DSL market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws. It is unclear at this juncture the extent to which linkLine is basing its § 2 price squeezing theory on wholesale pricing, retail pricing, or both. However, since linkLine could prove facts, consistent with its complaint, that involve only unregulated behavior at the retail level, its action or lawsuit survives a motion for judgment on the pleadings. We do not preclude the district court, however, from re-examining the viability of this claim on summary judgment after the record is more fully developed and it is clear whether the complained of behavior took place at the regulated wholesale level, the unregulated retail level, or some combination of the two, and to what extent, if any, the responsible agencies have devoted attention to or had involvement in the complained of conduct.[12] Based on the record

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[12] In *MetroNet*, we found relevant that the responsible agencies' "attentiveness to the alleged anticompetitive conduct." 383 F.3d 1124. In *Trinko* as well, both the FCC and the NYPSC had

before us at this time, we are able to conclude that the district court was correct to deny the SBC Entities' motion for judgment on the pleadings because linkLine's allegation that the pricing scheme created an anticompetitive price squeeze states a potentially valid claim under § 2 of the Sherman Act.

AFFIRMED.

GOULD, Circuit Judge, dissenting:

I respectfully dissent, concluding that the amended complaint should have been dismissed for failure to state a claim, in light of dispositive Supreme Court precedent, notwithstanding the permissive standard by which we assess a complaint when confronted with a motion to dismiss on the pleadings.

As the court correctly notes, we assume the facts pleaded in linkLine's amended complaint to be true. As a general matter it is not correct to dismiss the complaint if any facts might be proved under which the complaint would be valid. However, the complaint only generally alleges a "price squeeze" and related exclusionary conduct. The complaint does not allege that the SBC Entities had any market power to set or influence the retail price for internet service. So it seems quite odd to say they could have violated the antitrust laws in part because of retail pricing; if SBC has no power to set its retail prices above the price at which it has sold its wholesale connection, it does not make sense to consider its pricing an illegal "price squeeze" under the antitrust laws. Given that SBC's DSL internet connections

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already addressed Verizon's anticompetitive conduct. Where the regulatory agencies have failed to prevent or remedy anticompetitive conduct, the balance may tilt in favor of judicial intervention.

compete with connections by cable and by satellite, it is by no means clear that SBC has the market power to influence the retail market price.

Moreover, the complaint does not allege that the prices at which the SBC Entities sold retail "DSL" internet connections were below cost, under any measure of cost; yet to the extent the concern is with predation at the retail level, then it would seem that, in current antitrust theory, below-cost sales must be shown. The complaint does not allege that the SBC Entities, to the extent they had losses by selling below cost in the retail market, had any realistic prospect of recouping losses; yet again, this prospect of recoupment is an integral element of a predation analysis under current Supreme Court doctrine.

Because of the expense and burden of proceeding in the antitrust litigation, it would be inefficient and unwise to permit the complaint to proceed on the general allegations of price squeeze, absent allegation of critical facts that in my view are needed for liability. To put the matter practically, it seems to me that the Supreme Court's decision in *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) ("*Trinko*") in essence takes the issues of wholesale pricing out of the case, and thus transforms what is left of any claim of "price squeeze." If so, and if plaintiffs in good faith cannot allege market power, below cost sales and probable potential for recoupment in the retail market, then the case should not proceed. Conversely, if plaintiffs are able to allege that the SBC Entities had market power in the retail market to set or influence the price, and that their retail sales of internet connection were predatory in the sense of being below cost with a real prospect of

recoupment, then the case should proceed for factual development.[1] After *Trinko* and *Brooke Group v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993) ("*Brooke Group*"), the case doesn't get out of the antitrust law starting blocks if plaintiffs cannot make allegations showing that the retail prices charged by the SBC Entities were predatory in a sense forbidden by the antitrust laws.

The district court dismissed most of the allegations of the complaint, but let stand the "price squeeze" allegation. As the majority opinion notes, "At the time the amended complaint was filed, the SBC Entities were both a supplier to the Plaintiffs at the wholesale level, and a competitor at the retail level." The majority opinion also correctly explains: "In antitrust terms, a price squeeze occurs 'when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market.'" Yet, the notion of a "price squeeze" is itself in a squeeze between two recent Supreme Court precedents.

Let us look first at the part of the "price squeeze" represented by SBC setting the upstream price at which it would sell use of its land lines to linkLine and the other ISPs here suing. The Supreme Court's decision in *Trinko*, upholding the ability of a regulated monopolist to deal with a competitor on certain service terms, means that if SBC set its wholesale price, the upstream price, too high, that cannot be challenged under the antitrust laws by analogy to

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[1] It might then be resolved at the summary judgment stage if there were no genuine issue of material fact, but it would warrant trial if there were any disputed material fact issues.

permissible refusals to deal. I substantially and substantively agree with the position taken by the D.C. Circuit in *Covad Communications Co. v. Bell Atlantic Corp.*, wherein the court adopted the reasoning of a major treatise on antitrust law that "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Covad Commc'ns Co. v. Bell Atl. Corp.*, 398 F.3d 666, 673 (D.C.Cir.2005) (*quoting* 3A Areeda & Hovenkamp, Antitrust Law P767c3, at 129-30 (2d ed.2002)). I am in agreement with this reasoning so far as it goes: *Trinko* insulates from antitrust review the setting of the upstream price.

However, although the D.C. Circuit concluded from this that "price squeeze" allegations should be dismissed, in this respect I would disagree if the key allegations I have identified could be made, because part of the "price squeeze" allegation is based on the retail price set in the "downstream" market. Thus, here linkLine is complaining about its inability to buy use of wholesale service lines at the price set by SBC when it cannot compete with the retail price at which SBC itself sells DSL internet connections to consumers.

SBC's setting of its sale price of the use of its land lines by ISPs in a wholesale transaction cannot be the basis of an antitrust claim in light of *Trinko*. That, however, does not dispose of scrutiny of SBC's conduct in the retail market, for it is the price at which SBC sells DSL service to its retail customers that squeezes linkLine's ability to resell internet connections at a profit. Thus the "price squeeze" contention boils down to a claim of a predatory pricing on sales of internet connections by SBC in the retail market. If all that remains of the "price squeeze"

claim is a challenge to the retail prices set by SBC on sale of DSL internet connection service, then it seems to me essentially a predatory pricing claim, and it can only be viable in the first instance if the SBC Entities have some real market power sufficient to set or influence prices in the retail market.

Moreover, even beyond the need for alleging and proving some degree of market power in the retail market, if that is the true locus of the antitrust complaint after *Trinko*, the retail side of a price squeeze cannot be considered to create an antitrust violation if the retail pricing does not satisfy the requirements of *Brooke Group*, which set unmistakable limits on what can be considered to be predatory within the meaning of the antitrust laws. In that case the Supreme Court held that a predatory pricing claim could proceed only if there were allegations (1) that the prices set were below an appropriate measure of the seller's costs; and (2) that the seller had a reasonable prospect, or, under § 2 of the Sherman Act, a dangerous probability, of later recouping losses. *Id.* at 222-24. Here, plaintiffs in their "price squeeze" contentions in the amended complaint did not allege that the seller had the market power to set prices for internet connection in the retail market, that SBC's retail price, contributing to the squeeze, was set below cost, and that losses could later be recouped.

Because we have not heretofore held that there must be a showing of market power in the retail market, nor held that the standards of *Brooke Group* must be applied in assessing predation in the retail side of a "price squeeze," I do not think it would be correct to dismiss the complaint on the pleadings with prejudice. Instead, after dismissal, plaintiffs should have been free to amend their complaint

if they could assert in good faith the allegations that are requisite here, after *Trinko*, for antitrust liability.[2]

Thus I respectfully dissent, believing that the Supreme Court's precedents in *Trinko* and *Brooke Group* have so hemmed in the potential for "price squeeze" liability that the specific allegations I have identified are necessary to state an antitrust claim in the context of the "price squeeze" alleged.

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[2] There is just enough possibility of an injury occurring for reasons culpable under the antitrust laws, *see Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477 (1977), so that in my view, while the district court should have granted a motion to dismiss on the pleadings, the district court also should have permitted amendment in case the critical allegations can be made by the plaintiffs.

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

No. CV 03-5265 SVW (SHx)

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants.

[Filed Apr. 1, 2005]

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT'S MOTION TO STRIKE PORTIONS OF PLAINTIFF'S FIRST AMENDED COMPLAINT, TO DISMISS THE FIRST AMENDED COMPLAINT, OR TO CERTIFY OCTOBER 20, 2004, ORDER FOR INTERLOCUTORY APPEAL

I. Introduction.

On July 24, 2003, Plaintiffs linkLine Communications, Inc., Inreach Internet LLC, Om Networks d/b/a Omsoft Technologies, Inc., and Nitelog, Inc. d/b/a Red Shift Internet Services (collectively "Plaintiffs") filed this action for damages and injunctive relief against Defendants SBC California, Inc., Pacific Bell Internet Services, and SBC Advanced Solutions, Inc. (collectively "Defendants"). Plaintiffs allege, among

other causes of action, violations of Section 2 of the Sherman Act, 15 U.S.C. § 2.[1]

On October 20, 2004, this Court held that Plaintiffs' refusal-to-deal claim was barred by the Supreme Court's decision in *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004), but that Plaintiffs' price squeeze claim was not. The Court, however, did not rule on the viability of Plaintiffs' price squeeze claim. Instead, because the exact nature of Plaintiffs' price squeeze claim was unclear at the time, the Court directed Plaintiffs to file an amended complaint "limited to the price squeeze claim that details beyond the normal requirements of Rule 8 specific facts supporting Plaintiffs' price squeeze claim." Order, p. 33 [App., *infra*, 91a].

On December 7, 2004, Plaintiffs filed a First Amended Complaint for Damages and Injunctive Relief for Violations of Antitrust Laws and State Law Claims ("FAC"). In the FAC, Plaintiffs re-allege their claim that Defendants engaged in an unlawful price squeeze. (FAC ¶ 25(A).) In addition, Plaintiffs allege additional unlawful, anticompetitive acts which (according to Plaintiffs) demonstrate Defendants' specific intent to monopolize through a price squeeze. (FAC ¶ 25(B).) These acts include the precise acts which formed the basis of Plaintiffs' original refusal-to-deal claim and which this Court found could not

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[1] Plaintiffs seek damages and injunctive relief pursuant to Sections 4 and 16 of the Clayton Act, 15 U.S.C. §§ 15, 25. Plaintiffs also seek compensatory and exemplary damages for intentional interference with prospective economic advantage and restitution and injunctive relief for alleged unfair trade practices in violation of Section 17200 of the California Business and Professions Code.

constitute a viable refusal-to-deal claim under *Trinko*.

On January 14, 2005, Defendants filed Defendants' Motion to Strike Portions of Plaintiffs' First Amended Complaint, to Dismiss the First Amended Complaint, or to Certify October 29, 2004 Order for Interlocutory Appeal. Defendants seek to have the Court (1) strike the allegations contained in ¶ 25(B) from the FAC, (2) dismiss the FAC for failing to state a viable price squeeze claim, (3) or certify its October 20, 2005 Order for interlocutory appeal.

II. FACTS[2]

Defendant SBC California, Inc. ("SBC") (formerly known as Pacific Bell Telephone Company or Pac-Bell) has authority to operate as a local exchange carrier ("LEC"), providing local telephone services to California consumers within SBC's local service area. SBC is a subsidiary of SBC Communications, Inc. On September 17, 1998, SBC received approval from the California Public Utilities Commission ("CPUC"), in Resolution T-16191, to provide Digital Subscriber Line ("DSL") services to California consumers.

Defendant Pacific Bell Internet Services ("PBIS") is a subsidiary of SBC. Consumers who ordered SBC's DSL and chose PBIS as their ISP were billed the associated fee for Internet access on their regular monthly Pacific Bell telephone billing statement under the heading "Pacific Bell Internet Services."

Defendant SBC Advanced Solutions, Inc. ("SBC-ASI") is a subsidiary of SBC Communications, Inc., and an affiliate of SBC. In June 2000, responsibility for the provisioning and billing of DSL was transi-

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[2] As this is a motion to dismiss, the facts are taken from the FAC.

tioned from SBC to SBC-ASI and the CPUC granted SBC-ASI a certificate of public convenience and necessity to operate as a facilities-based provider of competitive local exchange and intraLATA interexchange services. SBC-ASI has since then provided DSL and other advanced services to independent ISPs and California consumers.

Plaintiffs are Internet Service Providers ("ISPs"). ISPs are commercial entities which provide consumers with access to the Internet. ISPs use a variety of telecommunications facilities to operate their portion of the Internet. Some ISPs own their own transmission and packet switching facilities, while others purchase or lease transmission or packet switches routers). Still others resell the facilities of other ISPs. Most often, ISPs will lease capacity to connect customers to the Internet.

Many ISPs sell "dial-up" services to customers. To provide this service, the ISPs obtain dedicated connections to local exchange carrier central office switches and then advertise their Internet telephone numbers to their subscribers who dial those numbers, reaching a bank of modems that are themselves connected to the ISP's portion of the Internet.

An increasingly popular alternative to dial-up is DSL. Many consumers prefer DSL because it is faster, "always on," more reliable, and allows simultaneous access by many users in the same area without affecting the speed or quality of the transmission. DSL can be made available over existing telephone lines. DSL service uses conventional voice network to carry digital information by means of a Digital Subscriber Line Access Multiplexer (DSLAM) placed in the central office and a modem placed at the end-users office or home. With a DSLAM at one end of

the traditional copper telephone loop and a modem at the other, it is possible to send bits of data at very high rates of speed.

For decades, local telephone companies have owned and controlled facilities that are essential to the provision of many telecommunications services, including DSL service. In most cases, the incumbent LEC (here SBC) owns and controls the connections to all or substantially all end user customers. ISPs that are not affiliated with the incumbent LEC must obtain access to those customer connections in order to reach and serve their own end user customers. In addition, non-affiliated ISPs often need to interconnect their own facilities with those of the incumbent LEC if they are to be able to provide communication services on a broad scale. Because of the critical nature of the incumbent LEC's network facilities, they are often referred to as "bottleneck" facilities. This is especially true of the "last-mile" connection between the incumbent LEC's central offices and the end-users' premises.

Because SBC is both an ISP (PBIS) and because SBC/SBC-ASI owns and controls the bottleneck facilities without which DSL cannot be provided, ISPs like Plaintiffs are in direct competition with the supplier of DSL transport services. While there are some locations where ISPs have a choice of DSL providers, the majority of wholesale DSL providers have ceased to operate in any significant geographic region of California, and SBC-ASI enjoys virtually exclusive control over DSL transport in SBC's service area (which covers approximately 78 percent of the geographic area of California). Moreover, because Defendants offer DSL services in wholesale and retail markets, they determine the cost of the critical

components of the competitor ISPs' service offerings. For instance, because PBIS combines DSL with both online services and equipment, which PBIS provides as a bundled package to end use customers, and because PBIS has taken in excess of 80 percent of the DSL market, independent ISPs are under competitive pressure to meet Defendants' prices and service combinations in the marketplace.

Plaintiffs allege that, beginning as early as mid-1998 and continuing up to the filing of Plaintiffs' Complaint, Defendants, acting as a single entity, have monopolized and attempted to monopolize, in violation of Section 2 of the Sherman Act, the relevant markets for providing DSL and other internet services and local telecommunication services in those geographic boundaries of Southern California where SBC is authorized to provide local exchange services.

In particular, Plaintiffs allege that Defendants have engaged in an unlawful price squeeze. Specifically, the FAC alleges that

> (1) . . . [D]efendants unlawfully manipulated their dual role as vertically integrated monopolists as both a wholesale-monopoly supplier and retail competitor of Plaintiffs by engaging in an unlawful price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which [D]efendants were providing retail DSL services and necessary equipment to end-user customers – and for a period by charging wholesale DSL prices to competing ISPs (such as [P]laintiffs) that actually exceeded the prices at which [D]efendants retail affiliate (PBIS) was charging retail end-user

customers for DSL services and necessary equipment – thereby making it impossible for independent ISP competitors such as plaintiffs to compete at the low retail prices set by [D]efendants' r combined DSL-Internet Service and n ary equipment provided to end-user customers.

(2) If [P]laintiffs charged retail DSL-Internet access customers the same retail price as [D]efendants' retail affiliate charged, [P]laintiffs could not cover the cost of providing DSL service, which costs necessarily includes the wholesale transport costs charged by [D]efendants.

(3) By the same token, if [D]efendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as [P]laintiffs), [D]efendants could not cover their wholesale costs and make a profit from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation), that were in some cases, and for some period, even below the wholesale DSL transport cost. Given the price margin relationship between retail and wholesale prices, [D]efendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as [P]laintiffs that are both wholesale customers and retail rivals.

(FAC ¶ 25(A)(1)-(3).) The FAC further alleges additional unlawful, anticompetitive acts which (according to the FAC) demonstrates Defendants' specific intent to monopolize. These acts include:

> (1) intentionally adopt[ing] anticompetitive procedures and processes for handling customer ordering and installation to ISPs that are calculated to (I) cause ISP customer disruption and interruption of service, and (ii) create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to [D]efendants;
>
> (2) purposefully creat[ing] and impos[ing] procedures and costs that impeded, and/or caused significant delays and costs for, end user customers of [D]efendants switching to the services of independent ISPs, including [P]laintiffs, and impos[ing] unreasonable and anticompetitive costs of DSL aggregation-backhaul circuits necessary for providing DSL service and particularly given the delays in processing orders, unfairly raised the per-customer costs of independent ISPs trying to compete with [D]efendants;
>
> (3) misle[ading], harass[ing], and exhibit[ing] hostility towards customers of ISPs, including [P]laintiffs;
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> (4) disparag[ing] and creat[ing] doubts about the efficacy and legality of ISPs, including [P]laintiffs; and
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> (5) purposefully fail[ing] to bill properly for DSL services.

(FAC ¶ 25(B)(1)-(5) .)

Plaintiffs claim that, as a result of Defendants' conduct, competition in the provision of DSL services and competition in the provision of Internet services has been effectively eliminated in Defendants' California service areas. Plaintiffs estimate their damages to be in excess of $40 million.

III. DISCUSSION

Defendants ask the Court to (1) strike the allegations set forth in ¶ 25(B) of the FAC on the grounds that they are the precise allegations dismissed by the Court in its October 20, 2004 Order, (2) dismiss Plaintiffs' price squeeze claim for failing to allege facts sufficient to state a claim of actual or attempted monopolization by price squeeze, and/or (3) certify its October 20, 2004 Order for interlocutory appeal.

A. Motion to Strike

Defendants move to strike the allegations set forth in ¶ 25(B) of the FAC on the ground that they are the precise allegations dismissed by the Court in its October 20 Order.[3] Plaintiffs oppose striking the allegations on the ground that they have evidentiary value on the issue of specific intent.

Rule 12(f) of the Federal Rules of Civil Procedure provides that the court "may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent, or scandalous material." Fed. R. Civ. P. 12(f). "Motions to strike are generally

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[3] The Court's October 20 Order dismissed the antitrust claims set forth in ¶ 23(b)-(f) of the original complaint. Despite this, Plaintiffs repeat those claims in ¶ 25(B)(1)-(5) of the FAC. In addition, ¶ 25(B)(2) contains an entirely new allegation pertaining to the pricing of DSL aggregation-backhaul circuits. Since the Court's October 20 Order limited Plaintiffs to re-alleging the previously dismissed price squeeze claim, Defendants request that the Court strike the new allegation.

disfavored." *FTC v. Medicor LLC*, 2001 WL 765628, at *2 (C.D. Cal. June 26, 2001). "Courts generally do not determine disputed or substantial questions of law on a motion to strike." *Id.* at *2. However, a 12(f) motion is proper when "it is clear that the matter to be stricken could have no possible bearing on the subject matter of the litigation." *LeDuc v. Ky. Cent. Life Ins.*, 814 F. Supp. 820, 830 (N.D. Cal. 1992). Nevertheless, "allegations supplying background or historical material or other matter of an evidentiary nature will not be stricken unless unduly prejudicial to defendant." *Id.* Thus, "[w]here allegations, when read with the complaint as a whole, give a full understanding [of the complaint], they need not be stricken." *Id.* However, where the plaintiff re-alleges claims that the court has already dismissed, the court may properly strike the previously dismissed claims. *See, e.g., Miller v. Continental Airlines, Inc.*, 2003 WL 21557678, at *2 (N.D. Cal. July 1, 2003) ("Plaintiffs' newly amended complaints contain exactly the same state law causes of action and claim for punitive damages previously dismissed with prejudice. . . . The renewed presence of these allegations in the amended complaints represents impertinent material."); *USS-Posco Indus. v. Contra Costa County Bldg. & Constr. Trades Council*, 721 F. Supp. 239, 242 (N.D. Cal. 1989) ("The current amended complaint is unacceptable because the first cause of action includes a restatement of several of the claims upon which summary judgment for defendants has already been granted by the Court. Plaintiffs may not allege in their amended complaint causes of action which have already been removed from this action by summary judgment, whether or

not they are asserted in combination with other valid or invalid claims.").

Defendants are correct that the allegations set forth in ¶ 25(B) of the FAC repeat the very allegations dismissed by this Court in its October 20 Order. However, the allegations need not be stricken if they have some relevance to Plaintiffs' price squeeze claim, whether as background or historical material or as matter of an evidentiary nature. Plaintiffs expressly claim that the allegations have evidentiary value on the issue of specific intent.[4] But as Defendants correctly note, *Trinko* held that allegations of insufficient assistance to rivals do not have any probative value as evidence of anticompetitive intent where there has been no prior course of voluntary dealings between the parties. *Trinko*, 540 U.S. at 409 ("The complaint does not allege that Verizon voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion. Here, therefore, the defendant's prior conduct sheds no light upon the motivation of its refusal to deal – upon whether its regulatory lapses were prompted not by competitive zeal but by anticompetitive malice."). The Court's October 20 Order dismissing Plaintiffs' refusal-to-deal claim was predicated on precisely this aspect of *Trinko*: since Plaintiffs had not alleged a prior course of voluntary dealings with Defendants, no inference of anticompetitive intent could be drawn from the allegations of insufficient assistance. The mere fact that

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[4] In *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373, 1378 (9th Cir. 1992), the Ninth Circuit imposed on plaintiffs alleging a price squeeze in a fully regulated industry the additional burden of pleading and proving that the defendant acted with specific intent

Plaintiffs are now attempting to use these allegations to buttress their price squeeze claim does not alter this analysis. Under *Trinko*, allegations of insufficient assistance to rivals can have no evidentiary value as to anticompetitive intent where the parties have not engaged in a prior course of voluntary dealings. It does not matter whether the underlying claim is a refusal-to-deal claim or, as here, a price squeeze claim. Thus, since the allegations contained in ¶ 25(B) of the FAC have no evidentiary value on the issue of anticompetitive intent, Plaintiffs' attempt to defend their inclusion on this ground fails. Consequently, the Court GRANTS the motion to strike.

B. Motion to Dismiss

Defendants move to dismiss Plaintiffs' price squeeze claim. Relying on the principles set forth in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), Defendants contend that the FAC fails to allege facts sufficient to state a claim of actual or attempted monopolization by price squeeze. Specifically, Defendants claim that the FAC does not sufficiently allege below-cost pricing or a dangerous probability of recoupment. Plaintiffs counter that the requirements set forth in *Brooke Group* do not apply to price squeeze claims and that, even if they did, the allegations contained in the FAC satisfy them.

To state a claim of monopolization under Section 2 of the Sherman Act, a plaintiff must allege that (1) the defendant possesses monopoly power in the relevant market; (2) the defendant has willfully acquired or maintained that power, and (3) the defendant's conduct has caused antitrust injury. *Cost Mgt. Servs., Inc. v. Washington Natural Gas Co.*, 99 F.3d

937, 949 (9th Cir. 1996). In *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373, 1378 (9th Cir. 1992), the Ninth Circuit imposed on plaintiffs alleging a price squeeze in a fully regulated industry the additional burden of pleading and proving that the defendant acted with specific intent. To state a claim of attempted monopolization under Section 2 of the Sherman Act, a plaintiff must allege: "(1) a specific intent to control prices or destroy competition; (2) predatory or anticompetitive conduct directed at accomplishing that purpose; (3) a dangerous probability of achieving 'monopoly power'; and (4) causal antitrust injury." *Image Technical Servs. v. Eastman Kodak Co.*, 125 F.3d 1195, 1202 (9th Cir. 1997) (quoting *Rebel Oil Co., Inc. v. Atlantic Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir. 1998)).

In order to survive a motion to dismiss under Rule 12(b)(6), "an antitrust complaint 'need only allege sufficient facts from which the court can discern the elements of an injury resulting from an act forbidden by the antitrust laws.'" *Cost Mgmt.*, 99 F.3d at 950 (quoting *Newman v. Universal Pictures*, 813 F.2d 1519, 1522 (9th Cir. 1987)). Whether a specific act or set of acts is anti-competitive is a question of law. *SmileCare Dental Group v. Delta Dental Plan of Cal., Inc.*, 88 F.3d 780, 783 (9th Cir. 1996). "Dismissal for failure to state a claim is appropriate where 'the complaint states no set of facts which, if true, would constitute an antitrust offense, notwithstanding its conclusory language regarding the elimination of competition and improper purpose.'" *Id.* (quoting *Rutman Wine Co. v. E. & J. Gallo Winery*, 829 F.2d 729, 735 (9th Cir. 1987)).

The issue here is whether the FAC states a viable price squeeze claim. Defendants contend that the

FAC does not state a viable price squeeze claim because Plaintiffs do not allege that Defendants were pricing below cost or that there was a dangerous probability that Defendants would recoup their investment. Defendants claim that these elements are required by the Supreme Court's decision in *Brooke Group*.

In *Brooke Group*, the Supreme Court held that there are two prerequisites to recovery when a plaintiff "alleges predatory pricing under § 2 of the Sherman Act or primary-line price discrimination under the Robinson-Patman Act." *Brooke Group*, 509 U.S. 222.[5] They are:

> First, a plaintiff seeking to establish competitive injury resulting from a rival's low prices must prove that the prices complained of are below an appropriate measure of its rival's costs. . . . The second prerequisite . . . is a demonstration that the competitor had a reasonable prospect, or, under § 2 of the Sherman Act, a dangerous probability, of recouping its investment in below-cost prices.

Id. at 222-24. The Court justified the first requirement on the ground that, as a general proposition, "the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting

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[5] Although *Brooke Group* involved a claim of primary-line price discrimination under the Robinson-Patman Act, the Court found that "primary-line competitive injury under the Robinson-Patman is of the same general character as the injury inflicted by predatory pricing schemes actionable under § 2 of the Sherman Act." *Id.* at 221.

intolerable risks of chilling legitimate price-cutting." *Id.* at 223. The Court justified the second requirement on the ground that, without recoupment, "predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced." *Id.* at 224.

Although the Court in *Brooke Group* did not hold that the two requirements applied to price squeeze claims, at least one court of appeals has applied them to price squeeze claims. *See Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050 (11th Cir. 2004) ("*Covad II*"). Moreover, although the Court in *Brooke Group* did not frame the requirements in terms of pleading standards, at least one court of appeals has applied the requirements to a motion to dismiss under Rule 12(b)(6). *See id.* (finding that the plaintiff's allegations stated a viable price squeeze under the *Brooke Group* requirements). As a threshold matter, this Court must decide whether it will follow the example of *Covad II*.

The court in *Covad II* provided no explanation for why it applied the *Brooke Group* requirements to the plaintiff's price squeeze claim. The failure of the court to explain its rationale for applying the *Brooke Group* requirements is surprising given the fact that the issue had been debated by the parties earlier in the litigation. *See Covad Communications Co. v. BellSouth Corp.*, 299 F.3d 1272, 1290-91 (11th Cir. 2002) ("*Covad I*"), *vacated*, 124 S. Ct. 1143 (2004).[6]

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[6] In *Covad I*, the defendant argued that the plaintiff was required to allege below-cost pricing. *Id.* at 1290. The defendant cited *Brooke Group* in support of its claim. *Id.* at 1291 n.17. In response, the plaintiff argued that "whether or not there is a price squeeze should not depend on whether retail prices are 'too low,' but rather on the 'squeeze' created by the disparity

Nonetheless, the Court's justification in *Brooke Group* for treating predatory pricing claims under Section 2 as analogous to primacy-line price discrimination claims under Robinson-Patman is so broad that it can be fairly read as applying with equal force to price squeeze claims.[7] After all, the essence of a price squeeze claim is that a rival has priced its products in an unfair manner with the object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market. Nonetheless, Defendants have not cited, and the Court has not found, any other case that applies the *Brooke Group* requirements to a price squeeze claim. For instance, in *Covad Communications Co. v. Pacific Bell*, 1999 WL 33757058, at *11 (N.D. Cal. Dec. 14, 1999), the court denied a motion to dismiss a price squeeze claim without discussing, much less applying, the *Brooke Group* requirements. Instead, the court denied the motion to dismiss on the ground that the plaintiff had alleged, in addition to an illegal price squeeze, "various forms of anti-competitive conduct," including "fraud, negligent misrepresentation, statutory and common law unfair competition, and interference with prospective economic advantage." *Id.* The court apparently viewed these allegations as

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between the wholesale prices [the plaintiff] must pay [the defendant] upstream and the prices [the plaintiff] must charge downstream to remain competitive with [the defendant]." *Id.* at 1291.

[7] The Court explained that "the essence of a claim under either statute [i.e., the Robinson-Patman Act and the Sherman Act] is the same: A business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market." *Brooke Group*, 509 U.S. at 222.

stating facts that, if true, would suffice as evidence of specific intent under *City of Anaheim*.

In light of the dearth of case law applying the *Brooke Group* requirements to price squeeze claims, this Court is reluctant to impose the *Brooke Group* requirements. Nevertheless, there are strong policy arguments for applying the *Brooke Group* requirements to price squeeze claims.

A price squeeze is, of course, structurally distinct from a predatory pricing scheme. The Supreme Court has defined predatory pricing as "pricing below an appropriate measure of cost for the purpose of eliminating competitors in the short run and reducing competition in the long run." *Cargill, Inc. v. Monfort of Colo.*, 479 U.S. 104, 117 (1986). Nothing in this definition requires that a firm operate at both the wholesale and retail level in order to engage in predatory pricing. By contrast, "[a] firm can engage in a price squeeze only if it operates both as a retailer and a wholesaler whose customers are also its competitors. A price squeeze occurs when that firm's price as a wholesaler is too high or as a retailer is too low for the competitor to stay in business." *CTC Communications Corp. v. Bell Atl. Corp.*, 77 F. Supp. 2d 124, 142 (D. Me. 1999). Thus, there is an undeniable structural distinction between a price squeeze and a predatory pricing scheme. But notwithstanding this distinction, it simply us [*sic*] not true, as Plaintiffs contend, that a price squeeze can be meaningfully distinguished from a predatory pricing scheme in terms of the anti-competitive harm or injury inflicted.[8] Plaintiff's reliance on the Ninth

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[8] Plaintiffs argue that the harm inflicted by a price squeeze inheres in the higher costs imposed upon the wholesale monopo-

Circuit's statement in *City of Anaheim* that "[t]he vice that a price squeeze has is that it can be used to cause severe damage to competitors by unjustifiably raising the costs of doing business," *City of Anaheim*, 955 F.2d 1373, is thus misplaced. As a statement of antitrust law, this statement *cannot* be taken as literally as Plaintiffs suggest. For as the Supreme Court and the Ninth Circuit has repeatedly emphasized, the antitrust laws exist to protect competition, not competitors. *See, e.g.*, *Brooke Group*, 509 U.S. 209 ("It is axiomatic that the antitrust laws were passed for 'the protection of competition, not competitors.'") (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962)); *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) ("The antitrust laws . . . were enacted for 'the protection of competition[,] not competitors.'") (quoting *Brown Shoe*, 370 U.S. at 320); *Brown Shoe*, 370 U.S. at 320 ("Taken as a whole, the legislative history [of the Sherman Act] illuminates congressional concern with the protection of competition, not competitors, and its desire to restrain mergers only to the extent that such combinations may tend to lessen competition."); *Or. Laborers-Employers Health & Welfare Trust Fund v. Philip Morris Inc.*, 185 F.3d 957, 966 (9th Cir. 1999) ("'The antitrust laws . . . were enacted for the protection of competition, not competitors.'") (quoting *Brunswick Corp.*, 429 U.S. at 488); *Adaptive Power Solutions, LLC v. Hughes Missile Sys. Co.*, 141 F.3d 947 (9th Cir. 1998) ("Antitrust laws are designed to protect competition, not competitors."); *Legal Econ. Evaluations, Inc. v. Metro Life Ins. Co.*, 39 F.3d 951 954 (9th Cir. 1994) ("The antitrust laws

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list's retail competitors, not the lower prices charged at the retail level by the wholesale monopolist.

were enacted for 'the protection of competition, not competitors.'") (quoting *Brown Shoe*, 370 U.S. at 320); *United States v. Syufy Enters.*, 903 F.2d 659, 668 (9th Cir. 1990) ("It can't be said often enough that the antitrust laws protect competition, not competitors."); *Oahu Gas Serv., Inc. v. Pac. Res., Inc.*, 838 F.2d 360, 370 (9th Cir.1988) ("The goal of the antitrust laws, however, unlike that of business tort or unfair competition laws, is to safeguard general competitive conditions, rather than to protect specific competitors."); *Hunt-Wesson Foods, Inc. v. Ragu Foods, Inc.*, 627 F.2d 919, 927 (9th Cir. 1980) ("Of course, it is free and open competition that the Sherman Act protects, and not any right of one competitor to be free of rough treatment at the hands of another."); *Ackerman-Chillingworth, Div. of Marsh & McLennan, Inc. v. Pac. Elec. Contractors Ass'n*, 579 F.2d 484, 492 (9th Cir. 1978) ("The Sherman Act protects competition, not competitors who may suffer some pecuniary harm because of the competitive process.").[9] Thus, the vice of a price squeeze cannot

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[9] *But see Hasbrouck v. Texaco, Inc.*, 842 F.2d 1034, 1040 (9th Cir. 1988) ("The oft-quoted chestnut distinguishing between protecting competition and protecting competitors has been misconstrued with some regularity by antitrust defendants who appear to argue in all types of antitrust cases that the effect of unlawful conduct on competitors is irrelevant. The purpose of drawing a distinction between harm to competition and harm to competitors is to point out that not all acts that harm competitors harm competition. However, the converse is not true. Injury to competition necessarily entails injury to at least some competitors. Competition does not exist in a vacuum; it consists of rivalry among competitors. Clearly, injury to competitors may be probative of harm to competition. . . . The aphorism may not be invoked blindly in response to a showing that competitors have been harmed; otherwise it would often serve to shield unlawful conduct that adversely affects competition.").

consist solely in the higher costs imposed upon the wholesale monopolist's retail competitors. (Nor, for that matter, can it consist solely in the lower retail prices charged by the wholesale-level monopolist.) Rather, a price squeeze is vicious only if the wholesale-level monopolist is able to achieve or has a dangerous probability of achieving dominant market position at the retail level as a result.[10] Absent this element, there is no reason to suppose that the damage done to the firm's retail competitors is, *ipso facto*, damage done to competition. As Areeda and Hovenkamp note, "It is critically important to realize that not all price squeezes are invidious. Most are not." 3 Phillip Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c, at 126 (2d ed. 2002). Indeed, Areeda and Hovenkamp note that a price squeeze may reflect five market realities, only the last of which raises a question of anti-competitive conduct: "(1) an adverse change in cost or demand conditions, (2) the elimination of monopoly profits at the second level, (3) the monopolist's increased efficiency, (4) indirect price discrimination, or (5) predatory pricing."

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[10] In this respect, the objective of a price squeeze is no different from that of predatory pricing. *Compare William Inglis & Sons Baking Co. v. ITT Continental Baking Co., Inc.*, 668 F.2d 1014, 1031-1032 (9th Cir. 1981) ("'Pricing is predatory only where the firm foregoes short-term profits in order to develop a market position such that the firm can later raise prices and recoup lost profits. . . .'") (quoting *Janich Bros., Inc. v. Am. Distilling Co.*, 570 F.2d 848, 856 (9th Cir. 1978)) *with Cities of Anaheim, Riverside, Banning, Colton & Asuza v. Fed. Energy Regulatory Comm'n*, 941 F.2d 1234, 1250 (D.C. Cir. 1991) ("[A] [p]rice squeeze occurs when a firm with monopoly power on the primary, or wholesale, level engages in a prolonged price increase that drives competitors out of the secondary, or retail, level, and *thereby extends its monopoly power to the secondary market*.") (emphasis added).

Id. at 126-27. Likewise, the First Circuit noted in *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 24 (1st Cir. 1990), that there are at least two circumstances in which a price squeeze may be beneficial. The first circumstance is where the wholesale-level monopolist is able to carry out its retail-level activities more efficiently than its independent competitors. *Id.* The second is where the retail-level firm being squeezed is itself a monopolist. *Id.* In light of these considerations, there are sound policy reasons for applying the *Brooke Group* requirements to price squeeze claims.[11]

Plaintiffs have offered two principal arguments against the application of the *Brooke Group* requirements to price squeeze claims. First, in the round of briefing which preceded the Court's October 20, 2004 Order, Plaintiffs argued that the *Brooke Group* requirements do not apply here because Plaintiffs' price squeeze claim is more analogous to a secondary-line price discrimination case. While it is true that *Brooke Group* does not, on its face, apply to secondary-line price discrimination claims[12], Plaintiffs'

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[11] It is important to note, however, that Areeda and Hovenkamp warn that a predatory price squeeze which consists in raising the wholesale price could be effected in some circumstances with little or no short-run loss of profits. Areeda & Hovenkamp, *Antitrust Law*, ¶ 767c5 at 129.

[12] Plaintiffs initially relied on *Chroma Lighting v. GTE Products Corp.*, 111 F.3d 653 (9th Cir. 1997), for this proposition. However, while it is true that the court in *Chroma Lighting* "decline[d] to extend the reasoning of *Brooke Group* to secondary-line cases because of the significant differences between primary- and secondary-line claims," *id.* at 658, *Chroma Lighting* involved a claim brought under the Robinson-Patman Act. Thus, the holding in *Chroma Lighting* is technically limited to cases brought under the Robinson-Patman Act. Moreover, the court's reasoning in *Chroma Lighting* does not

counsel acknowledged at the September 21, 2004 hearing that Plaintiffs' allegations are more analogous to a primary-line price discrimination claim. Given this admission and the fact that Plaintiffs abandoned this argument in the latest round of briefing, the Court will not address it.

Second, Plaintiffs argue that, in order to survive a motion to dismiss for failure to state a claim, a plaintiff alleging a price squeeze need only allege that the wholesale price was greater than the retail price. According to Plaintiffs, courts will presume an illegal price squeeze where the wholesale price was greater than the retail price. This test – known as the "comparative billing" test – was famously applied by the district court in *City of Mishawaka v. Am. Elec. Power Co., Inc.*, 465 F. Supp. 1320, 1328-1329 (N.D. Ind. 1979), *aff'd in part, vacated in part*, 616 F.2d 976 (7th Cir. 1980). However, the court in *Mishawaka* did not frame the test in terms of a presumption[13], and this Court is hard pressed to find any case authority for such a presumption. *See, e.g., Ray v.*

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justify expanding its holding to claims under Section 2. The court grounded its decision in the language and legislative history of the Robinson-Patman Act. *Id.* at 658. Thus, a fair reading of *Chroma Lighting* does not permit the expansive reading urged by Plaintiffs. However, an expansive reading of *Chroma Lighting* is not needed to limit *Brooke Group*'s holding. *Brooke Group* has already done that. As the First Circuit has noted, the holding of *Brooke Group* "on its face applies only to primary-line cases, not secondary-line cases." *Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp.*, 79 F.3d 182, 193 (1st Cir. 1996). The Court in *Brooke Group* specified that the two prerequisites applied to "claims alleging predatory pricing under § 2 of the Sherman Act or *primary-line* price discrimination under the Robinson-Patman Act." *Id.* at 222 (emphasis added).

[13] In fact, the court cited numerous other anti-competitive acts by the defendants. *Id.*

Ind. & Mich. Elec. Co., 606 F. Supp. 757, 777 (N.D. Ind. 1984) ("The court's decision in *City of Mishawaka v. American Electric Power Co.* does not require this court to refer the comparative billing test for a price squeeze. In that case the court found a price squeeze solely on the basis of such a test, but the court there was not presented with any alternative tests.").[14] In fact, the comparative billing test is only one of three tests used by courts. *See id.* at 776-77 (discussing the "comparative rate of return" test and the "transfer price" test). Thus, Plaintiffs' argument that "well established price squeeze authorities firmly support a free-standing basis for imposing Section 2 liability for cases . . . where wholesale prices were set higher than retail [prices]," Pl.'s Opp'n at 2, is simply unfounded.

Thus, the Court is inclined to apply the *Brooke Group* requirements to Plaintiffs' price squeeze claim. While the Court recognizes that there is a dearth of case law applying the *Brooke Group* requirements to price squeeze claims, the Court finds the policy arguments in favor of their application persuasive. Nevertheless, the Court concludes that it need not and should not resolve this difficult issue at this

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[14] In *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 808-09 (3d Cir. 1985), the court noted that the evidence showed that the price for aluminum pipe was "for a significant period of time in 1974" "just above, or even below" the price for aluminum coil but quickly added that "[t]he mere existence . . . of a 'price squeeze' is not necessarily an antitrust violation. The plaintiff must present evidence that the defendants deliberately produced the effect, sufficient to provide a reasonable basis for the jury to conclude that the 'squeeze' was not the result of natural market forces such as supply or demand or legitimate competition."

time.[15] First, the Court would benefit from further briefing and a fully developed factual record. Second, the Court finds that, even if the *Brooke Group* requirements were applied, the FAC would satisfy those requirements.

As noted above, the FAC alleges that

> (1) . . . [D]efendants unlawfully manipulated their dual role as vertically integrated monopolists as both a wholesale-monopoly supplier and retail competitor of Plaintiffs by engaging in an unlawful price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which [D]efendants were providing retail DSL services and necessary equipment to end-user customers – and for a period by charging wholesale DSL prices to competing ISPs (such as [P]laintiffs) that actually exceeded the prices at which [D]efendants retail affiliate (PBIS) was charging retail end-user customers for DSL services and necessary equipment – thereby making it impossible for independent ISP competitors such as plaintiffs to compete at the low retail prices set by [D]efendants for combined DSL-Internet Service and necessary equipment provided to end-user customers.
>
> (2) If [P]laintiffs charged retail DSL-Internet access customers the same retail price as [D]efendants' retail affiliate charged, [P]laintiffs could not cover the cost of providing DSL service, which costs necessarily includes the wholesale transport costs charged by [D]efendants.

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[15] The issue will thus be revisited at summary judgment.

> (3) By the same token, if [D]efendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as [P]laintiffs), [D]efendants could not cover their wholesale costs and make a profit from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation), that were in some cases, and for some period, even below the wholesale DSL transport cost. Given the price margin relationship between retail and wholesale prices, [D]efendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as [P]laintiffs that are both wholesale customers and retail rivals.

(FAC ¶ 25(A)(1)-(3) .)

While Defendants are correct that, strictly construed, the FAC falls short in a number of respects, the Court may not grant a motion to dismiss "unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). Here, Plaintiffs can clearly prove a set of facts in support of their price squeeze claim that would entitle them to relief.[16]

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[16] Moreover, as Plaintiffs note, the FAC contains price squeeze allegations substantially similar to those approved by the Court in *Covad II*.

While it is true that, as Defendants argue, subparagraphs (1) and (2) of ¶ 25(A) contain no allegation that Defendants' prices are below a relevant measure of Defendants' costs[17], subparagraph (3) contains something approximating an allegation of below-cost pricing. True, subparagraph (3) is not phrased as a factual allegation but as a conditional if-then statement, but Plaintiffs' counsel assured the Court at the February 28, 2005 hearing that the allegation of below-cost pricing was phrased in this way simply because Plaintiffs do not believe that they are required to allege below-cost pricing and did not wish to be bound to proving below-cost pricing. While less than satisfactory, Plaintiffs' counsel's explanation is credible.[18] Thus, the Court will not dismiss the FAC on this ground.

More problematic is the issue of whether the FAC adequately alleges a dangerous probability of recoupment. As Defendants note, nowhere in these paragraphs do Plaintiffs allege a dangerous probability of recoupment within the meaning of *Brooke Group*. As the Court explained in *Brooke Group*, for recoupment to occur, the predators "'must obtain enough market power to set higher than competitive prices, and then must sustain those prices long enough to earn in excess profits what they earlier gave up in below-cost prices.'" *Brooke Group*, 509 U.S. at 225-26 (quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 590-91 (1986)).

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[17] Instead, they allege only that Plaintiffs cannot make a profit by charging the retail prices Defendants charge.

[18] Because the applicability of the *Brooke Group* requirements to price squeezes had arisen in the first round of briefing, Plaintiff's counsel knew that Defendants would move to dismiss the FAC on this basis.

Stated otherwise, "[t]he plaintiff must demonstrate that there is a likelihood that the predatory scheme alleged would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation, including "the time value of the money invested in it." *Brooke Group*, 509 U.S. at 225. Nowhere in subparagraphs (1) through (3) do Plaintiffs allege that Defendants will be able, as a result of the alleged price squeeze, to obtain enough market power in the retail market in order to set supracompetitive prices for a sustained period of time. Instead, subparagraph (3) alleges only that Defendants are compensating for their low retail prices by setting their wholesale prices high. While Plaintiffs are correct that the *Covad II* court found such allegations sufficient under the second prong of *Brooke Group*, *see Covad II*, 374 F.3d at 1051 ("These allegations suggest that BellSouth is compensating for deliberately reduced profits on the retail end of its operations with correspondingly greater profits on the wholesale side, in order to stifle competition from firms such as Covad. . . . We find that these allegations are sufficient to allege a dangerous probability that BellSouth will recoup its investment in below-cost prices.") (internal quotations omitted), the simple fact is that such allegations do not suffice under *Brooke Group*. Under *Brooke Group*, recoupment must take the form of a sustained rise in prices sufficient for the would-be monopolist to recapture the income lost as a result of the earlier campaign of below-cost pricing. There is no such allegation here. Thus, subparagraph (3), standing alone, would not suffice under *Brooke Group*. Nonetheless, the FAC elsewhere alleges something akin to a dangerous probability of

recoupment within the meaning of *Brooke Group*. At ¶ 26(b), the FAC alleges that, as a result of Defendants' anti-competitive conduct, "competition in the provision of Internet services has been effectively eliminated in defendants' California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products." (FAC ¶ 26(b).) While this sentence does not explicitly allege supracompetitive pricing or that Defendants will be able to price at such a level for a sustained period of time, it suffices for pleading purposes.

C. Interloctuory Appeal

In the alternative, Defendants ask the Court to certify its October 20, 2004 Order for interlocutory appeal. Under 29 U.S.C. § 1292(b), a district judge may certify for interlocutory appeal an order not otherwise appealable if the judge is of the opinion the "order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order." 28 U.S.C. § 1292(b).

"Generally, interlocutory appeal should be granted 'sparingly.'" *A&J Deutscher Family Fund v. Bullard*, 1987 WL 16951, at *1 (C.D. Cal. March 25, 1987) (quoting *United States Rubber Co. v. Wright*, 359 F.2d 784, 785 (9th Cir. 1966)). "[T]he legislative history of 1292(b) indicates that this section was to be used only in exceptional situations in which allowing an interlocutory appeal would avoid protracted and expensive litigation." *In re Cement Antitrust Litig.*, 673 F.2d 1020, 1026 (9th Cir. 1982). Moreover, "district court judges have 'unfettered discretion' to deny

certification even when all three [statutory criteria] are satisfied." *Marshall v. City of Portland*, 2004 WL 1774532, at *1 (D. Or. Aug. 9, 2004).

1. *Controlling Question of Law*

An issue is "controlling" within the meaning of § 1292(b) if the "resolution of that issue on appeal could materially affect the outcome of the litigation in the district court." *In re Cement Antitrust Litig.*, 673 F.2d at 1026. A "question of law" generally means a "pure question of law." *Marshall*, 2004 WL 1774532, at *2; *but see Steering Comm. v. United States*, 6 F.3d 572 (9th Cir. 1993) (explaining that the presence of a pure question of law permits the court to resolve all questions, even mixed questions of law and fact, material to the order).

The question of whether *Trinko* bars price squeeze claims in a fully regulated industry is undoubtedly a pure question of law. And the resolution of this issue will materially affect the outcome of the instant litigation since a decision by the Ninth Circuit holding that price squeeze claims are barred under *Trinko* would terminate Plaintiffs' suit.

2. *Substantial Ground for Difference of Opinion*

In determining whether a "substantial ground for difference of opinion" exists, courts look at a variety of factors. For instance, while some courts have held that a substantial ground for difference of opinion is established by "a dearth of precedent within the controlling jurisdiction and conflicting decisions in other circuits," *APCC Servs., Inc. v. AT&T Corp.*, 297 F. Supp. 2d 101, 107 (D.D.C. 2003), other courts have held that a substantial ground for difference of opinion exists where the "issues are difficult and of first impression." *Klinghoffer v. S.N.C. Achille Lauro Ed*

Altri-Gestione Montonave Achille Lauro in Amministrazione Straordinaria, 921 F.2d 21, 25 (2d Cir. 1990); *but see In re Flor*, 79 F.3d 281, 284 (2d Cir. 1996) ("[T]he mere presence of a disputed issue that is a question of first impression, standing alone, is insufficient to demonstrate a substantial ground for difference of opinion."). However, most courts agree that the most important factor is "the strength of the arguments in opposition to the challenged ruling. . . ." *APCC Servs.*, 297 F. Supp. 2d at 107; *see also In re Flor*, 79 F.3d at 284.

Here, there is clearly a dearth of controlling precedent within the Ninth Circuit. Moreover, there is, as a result of *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. 2005), conflicting authority outside the Ninth Circuit.[19] While Plaintiffs argue that the facts in *Covad Communications* can be distinguished from those at issue here or in *Covad II*, the reality is that there is now a circuit split. This fact weighs in favor of granting Defendants' request that the Court certify its October 20 Order for interlocutory appeal.

More importantly, Defendants' arguments are strong. While the Court remains convinced that Defendants misread *Trinko* by conflating the first inquiry under *Trinko* (i.e., does the plaintiff's claim state a cognizable antitrust violation under existing antitrust standards?) with the second (i.e., should antitrust law be expanded to encompass plaintiff's claim?)[20], the Court recognizes that *Trinko* could be

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[19] In *Covad Communications*, the Court of Appeals for the District of Columbia Circuit concluded that *Trinko* barred the plaintiffs' price squeeze allegation. *Id.* at 673-74.

[20] In *Trinko*, the Court first determined whether the plaintiff's claim fell within the existing exceptions to the "no duty

interpreted differently. Moreover, there is persuasive appeal to Defendants' argument that the underlying logic of *Trinko*, which is that no inference of anticompetitive intent can be drawn from a refusal to deal where the parties are compelled by law to deal, applies with equal force to price squeeze claims since a price squeeze claim is, in essence, a claim that the wholesale-level monopolist is not dealing with its retail-level competitors on the competitors' preferred terms. The Court rejected this argument in its October 20 Order on the ground that *Trinko* specifically held that it did not apply to antitrust claims which are cognizable under existing case law. But as Defendants point out, price squeeze claims are no more well established under existing case law than are refusal-to-deal claims.[21] Thus, although the

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to deal" rule. *Trinko*, 540 U.S. at 407-11. Only then did the Court examine whether traditional antitrust principles (i.e., the policies underlying antitrust law) justified adding the plaintiff's claim to the existing body of cognizable antitrust claims. *Id.* at 411-15. The Ninth Circuit employed precisely this analytical framework in *Metronet Services Corp. v. Qwest Corp.*, 383 F.3d 1124 (2004). First, the court discussed whether the plaintiff's claim fell within the existing exceptions to the "no duty to deal" rule. *Id.* at 1130-34. Only then did it examine whether it should expand the contours of Section 2 liability in order to accommodate the plaintiff's claim. *Id.* at 1134-37. It was at this point that the court "weigh[ed] the 'benefits of antitrust intervention' against 'a realistic assessment of its costs.'" *Id.* at 1134. Here, Defendants are conflating these two inquiries, asking the Court to preclude Section 2 liability in a fully regulated industry even under existing antitrust law because the costs of such regulation outweigh its benefits. *Trinko* did not announce such a wholesale rethinking of antitrust law.

[21] The Court remains convinced that this argument misconstrues *Trinko*. The first inquiry under *Trinko* is not whether a particular type of antitrust claim is well established but whether the plaintiff states a claim under existing antitrust

Court remains firmly convinced that it decided the issue correctly, it recognizes that Defendants arguments are sufficient to establish that a substantial ground for difference of opinion exists.

3. *Resolution of the Issue Would Materially Advance the Ultimate Termination of the Litigation*

For the reasons explained above, there can be no doubt that the resolution of this issue would materially advance the ultimate termination of the litigation. Thus, the Court GRANTS Defendants' request that the Court certify its October 20 Order for interlocutory appeal.[22]

IV. CONCLUSION

Because the allegations set forth in ¶ 25(A) of the FAC can have no evidentiary value on the issue of anticompetitive intent under *Trinko*, the Court GRANTS Defendants' Motion to Strike Portions of Plaintiffs' First Amended Complaint [27]. However, because the Court finds that the FAC, generously construed, would state a valid price squeeze claim under *Brooke Group*, the Court DENIES Defendants' Motion to Dismiss the First Amended Complaint [27]. Finally, because the question of whether *Trinko* bars price squeeze claims where the parties are compelled to deal under the federal communications laws

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case law, whether or not that particular type of claim is well established.

[22] In light of the Court's holding that the FAC can be read to state a viable price squeeze claim under *Brooke Group*, the issue before the Ninth Circuit will not only be whether *Trinko* bars price squeeze claims generally but, more specifically, whether it bars predatory price squeeze claims (i.e., price squeeze claims which comply with the *Brooke Group* requirements).

is a controlling question of law about which there is a substantial ground for difference of opinion, and because a resolution of this issue could potentially spare the parties considerable time and expense in protracted discovery, the Court GRANTS Defendants' Motion to Certify October 20, 2004, Order for Interlocutory Appeal [27].

IT IS SO ORDERED.

Dated: 3/31/05 /s/ STEPHEN V. WILSON
STEPHEN V. WILSON
UNITED STATES DISTRICT JUDGE

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

No. CV 03-5265 SVW (SHx)

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants.

[Filed Oct. 20, 2004]

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANTS' MOTION FOR JUDGMENT ON THE PLEADINGS

TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

I. INTRODUCTION/FACTUAL[1] & PROCEDURAL HISTORY

Plaintiffs linkLine Communications, Inc., Inreach Internet LLC, Om Networks d/b/a Omsoft Technologies, Inc., and Nitelog, Inc. d/b/a Red Shift Internet Services filed this action for damages and injunctive relief against Defendants SBC California, Inc., Pacific Bell Internet Services, and SBC Advanced Solutions, Inc. on July 24, 2004. Plaintiffs allege,

[1] As this is a motion for judgment on the pleadings, the facts are taken from the Complaint's allegations.

among other causes of action, violations of Section 2 of the Sherman Act, 15 U.S.C. § 2.[2]

Defendant SBC California, Inc. ("SBC") has authority to operate as a local exchange carrier ("LEC"), providing local telephone services to California consumers within PacBell's local service area. (Complaint ¶ 7.) SBC is a subsidiary of SBC Communications, Inc. (Complaint ¶ 7.) On September 17, 1998, SBC received approval from the California Public Utilities Commission ("CPUC"), in Resolution T-16191, to provide Digital Subscriber Line ("DSL") services to California consumers. (Complaint ¶ 7.)

Defendant Pacific Bell Internet Services ("PBIS") is a subsidiary of SBC. (Complaint ¶ 8.) Consumers who ordered SBC's DSL service and chose PBIS as their Internet Service Provider ("ISP") were billed the associated fee for Internet access on their regular monthly Pacific Bell telephone billing statement under the heading "Pacific Bell Internet Services." (Complaint ¶ 8.)

Defendant SBC Advanced Solutions, Inc. ("SBC-ASI") is a subsidiary of SBC Communications, Inc., and an affiliate of SBC. (Complaint ¶ 9.) In June 2000, responsibility for the provisioning and billing of DSL was transitioned from SBC to SBC-ASI and the CPUC granted SBC-ASI a certificate of public convenience and necessity to operate as a facilities-based provider of competitive local exchange and intraLATA interexchange services. (Complaint ¶ 9.)

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[2] Plaintiffs seek damages and injunctive relief pursuant to Sections 4 and 16 of the Clayton Act, 15 U.S.C. §§ 15, 25. Plaintiffs also seek compensatory and exemplary damages for intentional interference with prospective economic advantage and restitution and injunctive relief for alleged violations of Section 17200 of the California Business and Professions Code.

SBC-ASI has since then provided DSL and other advanced services to independent ISPs and California consumers. (Complaint ¶ 9.)

Plaintiffs are independent ISPs. (Complaint ¶¶ 3-5.) ISPs provide access to the Internet and related services. (Complaint ¶ 15.) ISPs use a variety of telecommunications facilities to operate their portion of the Internet. (Complaint ¶ 15.) Some ISPs own their own transmission and packet switching facilities while others purchase or lease transmission or packet switches (routers). (Complaint ¶ 15.) Still others resell the facilities of other ISPs. (Complaint ¶ 15.)

Most often, ISPs will lease capacity to connect customers to the Internet. (Complaint ¶ 15.) Many ISPs sell "dial-up" services to customers. (Complaint ¶ 16.) To provide this service, the ISP obtains dedicated connections to local exchange carrier central office switches and then advertises its Internet telephone numbers to its subscribers who dial those numbers, reaching a bank of modems that are themselves connected to the ISP's portion of the Internet. (Complaint ¶ 16.)

An increasingly popular alternative to dial-up is DSL. (Complaint ¶ 17.) Many consumers prefer DSL because it is faster, "always on," more reliable, and allows simultaneous access by many users in the same area without affecting the speed or quality of the transmission. (Complaint ¶ 11.) DSL can be made available over existing telephone lines. (Complaint ¶ 11.) DSL service uses conventional voice network to carry digital information by means of a Digital Subscriber Line Access Multiplexer (DSLAM) placed in the central office and a modem placed at the end-users office or home. (Complaint

¶ 17.) With a DSLAM at one end of the traditional copper telephone loop and a modem at the other, it is possible to send bits of data at very high rates of speed. (Complaint ¶ 17.)

For decades, local telephone companies have owned and controlled the facilities that are essential to the provision of many telecommunications services, including DSL service. (Complaint ¶ 18.) In most cases, the incumbent LEC (here SBC) owns and controls the connections to all or substantially all end user customers. (Complaint ¶ 18.) ISPs that are not affiliated with the incumbent LEC must obtain access to those customer connections in order to reach and serve their own end user customers. (Complaint ¶ 18.) In addition, non-affiliated ISPs often need to interconnect their own facilities with those of the incumbent LEC if they are to be able to provide the communication services on a broad scale. (Complaint ¶ 18.) Because of the critical nature of the incumbent LEC's network facilities, they are often referred to as "bottleneck" facilities. (Complaint ¶ 18.) This is especially true of the "last-mile" connection between the incumbent LEC's central offices and the end-users' premises. (Complaint ¶ 18.)

Because SBC is also an ISP (PBIS) and because SBC/SBC-ASI owns and controls the bottleneck facilities without which DSL cannot be provided, ISPs, including Plaintiffs, are in direct competition with the supplier of DSL transport services. (Complaint ¶ 18.) While there are some locations where ISPs have a choice of DSL providers, the majority of wholesale DSL providers have ceased to operate in any significant geographic region of California, and SBC-ASI enjoys virtually exclusive control over DSL transport in SBC's service area (which covers

approximately 78 percent of the geographic area of California). (Complaint ¶ 18.) Moreover, because Defendants offer DSL services in wholesale and retail markets, they determine the cost of the critical components of the competitor ISPs' service of offerings. (Complaint ¶ 19.) For instance, because PBIS combines DSL with both online services and equipment, which PBIS provides as a bundled package to end use customers, and because PBIS has taken in excess of 80 percent of the DSL market, independent ISPs are under competitive pressure to meet Defendants' prices and service combinations in the marketplace. (Complaint ¶ 19.) When the wholesale-retail margin is set artificially low, ISPs are placed at a serious disadvantage vis-a-vis the vertically integrated SBC entities. (Complaint ¶ 19.)

Plaintiffs allege that, beginning as early as mid-1998 and continuing up to the filing of Plaintiffs' complaint, Defendants, acting as a single entity, have monopolized and attempted to monopolize, in violation of Section 2 of the Sherman Act, the relevant markets for providing DSL and other internet services and local telecommunication services in those geographic boundaries of Southern California where SBC is authorized to provide local exchange services. (Complaint ¶ 22.)

In particular, Plaintiffs allege that Defendants have committed the following unlawful acts in order to maintain its existing DSL/ISP and local telecommunication service monopolies and to exclude and unreasonably impede competition from independent ISPs:

> (a) created a price squeeze by charging ISPs a high wholesale price in relation to the price

at which Defendants were providing retail services;

(b) intentionally adopted anticompetitive procedures and processes for handling customer ordering and installation that are calculated to cause ISP customer disruption and interruption of service and create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to Defendants;

(c) purposefully created and imposed procedures that impeded, and/or caused significant delays and costs for end user customers of Defendants switching to the services of independent ISPs;

(d) misled, harassed and exhibited hostility toward customers of ISPs, including Plaintiffs' customers;

(e) disparaged and created doubts about the efficiency and legality of ISPs, including Plaintiffs'; and

(f) purposefully failed to bill properly for DSL services.

(Complaint ¶ 23(a)-(f).)

Plaintiffs claim that, as a result of Defendants' conduct, competition in the provision of DSL services and competition in the provision of Internet services has been effectively eliminated in Defendants' California service areas. (Complaint ¶ 24(a)-(b).) Plaintiffs estimate their damages to be in excess of $40 million. (Complaint ¶ 26.)

On July 6, 2004, Defendants filed a Notice of Motion and Motion for Judgment on the Pleadings. That Motion is now before the Court.[3]

II. JUDGMENT ON THE PLEADINGS

Federal Rule of Civil Procedure 12(c) provides that "[a]fter the pleadings are closed but within such time as not to delay the trial, any party may move for judgment on the pleadings." Fed. R. Civ. P. 12(c). "A Rule 12(c) motion challenges the legal sufficiency of the opposing party's pleadings." *Benas v. Baca*, 2001 WL 485168, at *2 (C.D. Cal. April 23, 2001). "In reviewing Rule 12(c) motions, the court must assume the truthfulness of the material facts alleged in the complaint and draw all reasonable inferences in favor of the nonmoving party." *Id.* A "district court may grant a motion for judgment on the pleadings 'when the moving party clearly establishes on the face of the pleadings that no material issue of fact remains to be resolved and that it is entitled to judgment as a matter of law.'" *Yanez v. United States*, 63 F.3d 870, 872 (9th Cir. 1995) (quoting *Hal Roach Studios, Inc. v. Richard Feiner & Co., Inc.*, 896 12 F.2d 1542, 1550 (9th Cir. 1989)). But "[j]udgment 'may only be granted when the pleadings show that it is "beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief."'" *Enron Oil Trading & Transp. v. Walbrook Ins. Co.*, 132 F.3d 526, 529 (9th Cir. 1997) (quoting *B.F. Goodrich v. Betkoski*, 99 F.3d 505, 529 (2d Cir. 1996) (quoting *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957))). A judgment on the pleadings is reviewed de novo. *Yanez*, 63 F.3d at 872.

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[3] On September 21, 2004, the Court heard extensive argument from the parties regarding Defendants' Motion.

III. DISCUSSION

The issue before the Court is whether, in light of the Supreme Court's decision in *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 124 S. Ct. 872 (2004), Plaintiffs can state a claim of monopolization or attempted monopolization in violation of Section 2 of the Sherman Antitrust Act.[4] Defendants contend that *Trinko* is directly on point and compels judgment in their favor. Plaintiffs claim *Trinko* is distinguishable and thus inapplicable. There is merit to both arguments.

A. *Trinko*

In *Trinko*, a customer of a rival of Verizon Communications, Inc. ("Verizon") sued Verizon, alleging that Verizon had filled rivals' orders on a discriminatory basis as part of an anticompetitive scheme to discourage customers from becoming or remaining customers of competitive LECs, thus impeding the ability of the competitive LECs to enter and compete in the market for local telephone service. *Id.* at 877. The complaint identified a single example of Verizon's allegedly anticompetitive conduct: a failure by Verizon to provide competitive LECs adequate access to its operations support systems ("OSS"), a set of systems used by incumbent LECs to provide services to customers and ensure quality. *Id.*

Under the Telecommunications Act of 1996, Pub.L. 104-104, 110 Stat. 56, incumbent LECs like Verizon have a duty to share their networks with competitors. *Id.* at 877-78. In particular, Section 251(c) of the Act requires LECs to offer access to unbundled network elements (UNEs) on "just, reasonable, and

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[4] The viability of Plaintiffs' state law claims are not presently before the Court.

nondiscriminatory" terms. *Id.* at 878 (quoting 47 U.S.C. § 251(c)(3)).[5] As part of its UNE obligations under Section 251(c)(3), Verizon was required to provide competitive LECs with access to its OSS. *Id.* at 876.[6] Access to OSS is crucial to a competitive LEC's viability because it cannot fill its orders without such access. *Id.* Even before the plaintiff filed suit against Verizon over its alleged failure to provide adequate OSS access, Verizon's conduct had been investigated by the Federal Communications Commission (FCC) and New York's Public Services Commission (PSC). *Id.* at 876. The investigation led to a series of orders by the PSC and a consent decree with the FCC. *Id.*

Pointing to the conduct at issue in the FCC and PSC investigations, the Law Offices of Curtis V. Trinko, LLP ("Trinko"), a customer of one of Verizon's rivals, filed suit against Verizon, claiming that Verizon denied services to its rivals in order to limit entry. *Id.* at 878. The Court construed Trinko's claim as a refusal-to-deal allegation under Section 2 of the Sherman Act. *Id.* at 879. The issue before the

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[5] The Act defines a "network element" as

> a facility or equipment used in the provision of a telecommunications service. Such term also includes features, functions, and capabilities that are provided by means of such facility or equipment, including subscriber numbers, databases, signaling systems, and information sufficient for billing and collection or used in the transmission, routing, or other provision of a telecommunications service.

47 U.S.C. § 153(29).

[6] The Supreme Court had previously upheld the FCC's treatment of OSS as a "network element" subject to the UNE obligations imposed on incumbent LECs under Section 251(c)(3). *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 386-87 (1999).

Court was whether the conduct alleged in Trinko's complaint was sufficient to state a viable refusal-to-deal claim.

While the Supreme Court has long acknowledged the "right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal," *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919), the Court has also made it clear that the right is "neither absolute nor exempt from regulation." *Lorain Journal Co. v. United States*, 342 U.S. 143, 155 (1951). Beginning with *Eastman Kodak Co. v. S. Photo Materials Co.*, 273 U.S. 359 (1927), the Court has found that, under certain circumstances, a firm's refusal to deal can have evidentiary value" or "give rise to liability." *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 601 (1985).

The most notable refusal-to-deal case prior to *Trinko* was *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.* In *Aspen*, the plaintiff, who owned one of four mountain areas, and the defendant, who owned the other three, had cooperated for years in the sale of a joint, multiple-day, all-area ticket that gave skiers access to all four mountains. *Id.* at 587-92. Eventually, the defendant decided to discontinue the joint tickets. *Id.* at 592-93. The plaintiff even offered to buy the lift tickets from the defendant at retail, but the defendant refused. *Id.* at 593. The plaintiff filed suit against the defendant, alleging that the defendant's actions violated Section 2 of the Sherman Act. *Id.* at 595. The case was tried to a jury, which returned a verdict for the plaintiff. *Id.* On appeal, the Supreme Court upheld the jury's verdict, finding the evidence sufficient to support it. *Id.*

at 610-11. In the process, the Court reaffirmed its commitment to the proposition that "[t]he high value that we have placed on the right to refuse to deal with other firms does not mean that the right is unqualified." *Id.* at 601.

In *Trinko* the Court revisited its decision in *Aspen*. Rejecting Trinko's broad reading of *Aspen*, the Court described the case as "at or near the outer boundary of § 2 liability." *Trinko*, 124 S. Ct. at 879. While acknowledging that "a refusal to cooperate with rivals can constitute anticompetitive conduct and violate § 2" under certain circumstances, the Court noted that "[w]e have been very cautious in recognizing such exceptions. . . ." *Id.* The Court then proceeded to distinguish the conduct at issue in *Aspen* from that at issue in *Trinko*. In *Aspen*, the defendant unilaterally terminated "a voluntary (*and thus presumably profitable*) course of dealing. . . ." *Id.* at 880 (emphasis in original). In the Court's view, this "suggested a willingness to forsake short-term profits to achieve an anticompetitive end." *Id.* Similarly, the defendant in *Aspen* refused to sell lift tickets to the plaintiff "*even if compensated at retail price*." *Id.* (emphasis in original). To the *Trinko* Court, this "revealed a distinctly anticompetitive bent." *Id.* In contrast, Trinko did not "allege that Verizon voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion." *Id.* Thus, unlike the defendant's conduct in *Aspen*, Verizon's "prior conduct sheds no light upon the motivation of its refusal to deal – upon whether its regulatory lapses were prompted not by competitive zeal but by anticompetitive malice." *Id.* Moreover, while the product the defendant refused to offer the plaintiff in *Aspen* was "a product that it already sold at

retail," "the services allegedly withheld [by Verizon] are not otherwise marketed or available to the public. The sharing obligation imposed by the 1996 Act created 'something new' – 'the wholesale market for leasing network elements.'" *Id.* (quoting *Verizon Communications Inc. v. FCC*, 533 U.S. 467, 528 (2002)).[7] Thus, the Court distinguished Trinko's refusal-to-deal claim from the plaintiff's in *Aspen* on the basis of two factors: 1) Verizon was not engaged in a voluntary course of dealing with its rivals and 2) the services Verizon was required to offer it rivals would not have been available to outside entities or members of the public absent statutory compulsion.[8] Given these differences, the Court concluded that "Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust

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[7] The Court dwelled on the fact that the services were previously unavailable – and indeed inaccessible – to outside entities:

> The unbundled elements offered pursuant to § 251(c)(3) exist only deep within the bowels of Verizon; they are brought out on compulsion of the 1996 Act and offered not to consumers but to rivals, and at considerable expense and effort. New systems must be designed and implemented simply to make that access possible – indeed, it is the failure of one of those systems that prompted the present complaint.

Id.

[8] The third factor – the fact that there was no conduct on Verizon's part analogous to the *Aspen* defendant's refusal to sell lift tickets to the plaintiff at the prevailing retail price – was not central to the Court's decision. Nonetheless, the Ninth Circuit has identified it as one of three factors the *Trinko* Court relied upon to distinguish Trinko's claim from that of the *Aspen* plaintiff. *MetroNet Servs. Corp. v. Qwest Corp.*, 2004 WL 2125769, at *6-8 (9th Cir. Sept. 24, 2004).

claim under this Court's existing refusal-to-deal precedents." *Id.* at 880.

Finally, although it pointedly declined to analyze Trinko's claim as an essential-facilities claim[9], the Court explained that its "conclusion would be unchanged even if we considered to be established law the 'essential facilities' doctrine crafted by some lower courts. . . ." *Id.* at 880. The Court argued that the "indispensable requirement for invoking the doctrine is the unavailability of access to the 'essential facilities,'" *id.* at 881, and that, by virtue of "[t]he 1996 Act's extensive provision for access," *id.*, that requirement was not met here. Thus, the Court concluded that, even if it had analyzed Trinko's claim as an essential-facilities claim, it would have failed.

B. *Trinko's Meaning*

It is important at the outset to be clear about what *Trinko* does and does not stand for. While *Trinko* is clearly a decision with broad implications, its implications are not unbounded. First, as the Court noted in *Trinko*, the Telecommunications Act of 1996 "preserves claims that satisfy existing antitrust standards. . . ." *Id.* at 878. Thus, it would be a serious misreading of *Trinko* to say that it shields regulated telecommunications companies from Section 2 liability for violations of the 1996 Act. Rather, *Trinko* holds that regulated telecommunications companies are not liable for conduct that, while actionable under the telecommunications law, does *not* violate existing antitrust standards. The Court, in other words, simply held that violations of the 1996 Act are not, *ipso facto*, violations of Section 2. Nonetheless,

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[9] The Court noted that it had "never recognized such a doctrine." *Id.* at 881.

a violation of the 1996 Act may, under certain circumstances, also violate Section 2.[10] Second, while *Trinko*'s holding is not limited to its facts, its holding is not unmoored from its facts. Thus, it is simply not true that *Trinko* immunizes regulated telecommunication companies from Section 2 liability for refusals to deal with a competitor. Rather, *Trinko* holds that a regulated telecommunications company cannot be liable under Section 2 for refusing to deal where its only dealings with the plaintiff were, from the start, compelled by the telecommunications laws.[11]

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[10] *See, e.g., Cavalier Tel., LLC v. Verizon Va., Inc.*, 330 F.3d 176, 189 (4th Cir. 2003), *cert. denied*, 124 S. Ct. 1144 (2004) ("We must remain clear . . . that even as we conclude that the Telecommunications Act and the Sherman Act impose independently enforceable duties, we do not conclude that every complaint that states violations of §§ 251 and 252 of the Telecommunications Act cannot for that reason alone also state a claim for violations of the Sherman Act. In circumstances where facts state a claim under both statutes construed independently of each other, they may give rise to relief under each act.").

[11] An argument could be made that *Trinko*'s holding is even narrower than this. Indeed, the Court in *Trinko* seemed to leave open the possibility that a claim like Trinko's might survive if the plaintiff were to plead facts that, if proven, would be sufficient to show that the defendant *would have* done business with the plaintiff even absent statutory compulsion. *Trinko*, 124 S. Ct. at 880 (faulting Trinko's complaint for "not alleg[ing] that Verizon voluntarily engaged in a course of dealing with its rivals, *or would ever have done so absent statutory compulsion*.") (emphasis added). However, it is difficult to envision what facts, absent a history of prior voluntary dealings, would be sufficient to make such a showing. This is undoubtedly why some courts have read *Trinko* as requiring a prior history of voluntary dealings. *See Covad Communications v. BellSouth Corp.*, 374 F.3d 1044, 1049 (11th Cir. 2004) ("*Trinko* now effectively makes the unilateral termination of a voluntary course of

In *Z-Tel Communications, Inc. v. SBC Communications, Inc.*, 2004 WL 1775940 (E.D. Tex. Aug. 6, 2004), this distinction proved crucial. In that case, the competitive LEC alleged that the incumbent LEC "voluntarily shared its network before the enactment of the 1996 Act." *Id.* at *9. The court found these allegations sufficient to state a claim under Section 2 notwithstanding *Trinko* because "a viable cause of action may proceed in harmony with *Trinko*" "if an antitrust plaintiff's contention of voluntary (i.e., pre-statutory compulsion) network is substantiated." *Id.*; *see also Nobody in Particular Presents, Inc. v. Clear Channel Communications, Inc.*, 311 F. Supp. 2d 1048, 1113 (D. Colo. 2004) (noting that, unlike Verizon, Clear Channel had previously engaged in voluntary dealings with the plaintiff). Thus, careful attention to the particular facts alleged by an antitrust plaintiff is essential where the defendant invokes *Trinko*.[12]

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dealing a requirement for a valid refusal-to-deal claim under *Aspen*.").

[12] It should also be noted that *Trinko* does not address the viability of Section 2 claims involving violations of the 1996 Act where *concerted* action is alleged. Indeed, the Court explicitly distinguished *United States v. Terminal Railroad Association of St. Louis*, 224 U.S. 383 (1912), and *Associated Press v. United States*, 326 U.S. 1 (1945), from the conduct alleged by Trinko on the ground that those cases "involved *concerted* action, which presents greater anticompetitive concerns and is amendable to a remedy that does not require judicial estimation of free-market forces: simply requiring that the outsider be granted nondiscriminatory admission to the club." *Id.* at 880 n.3 (emphasis in original). Thus, it remains an open question whether *Trinko* forecloses Section 2 claims against regulated telecommunications companies where the plaintiff alleges a conspiracy or combination.

C. *Trinko's Progeny*

Three recent cases illustrate *Trinko*'s impact.

1. *Covad*

In *Covad Communications Co. v. BellSouth Corp.*, 299 F.3d 1272, 1276-78 (11th Cir. 2002), *vacated*, 124 S. Ct. 1143 (2004), a pre-*Trinko* case, the plaintiff ISPs filed suit against the defendant, an incumbent LEC, alleging that the defendant had violated the terms of the interconnection agreement the parties had entered into and engaged in anticompetitive conduct aimed at trying to impede or delay plaintiffs' entry into the DSL market. The district court dismissed the plaintiffs' complaint, finding that it had not stated a cognizable antitrust claim. *Id.* On appeal, the Eleventh Circuit reversed, finding that plaintiffs' complaint alleged three forms of recognized anticompetitive conduct: refusal to deal, essential facilities, and price squeezing. *Id.* at 1284-1291. However, following its decision in *Trinko*, the Supreme Court vacated the Eleventh Circuit's decision and remanded the case for further consideration in the light of *Trinko*. *BellSouth Corp. v. Covad Communications Co.*, 124 S. Ct. 1143 (2004). On remand, the Eleventh Circuit dismissed the plaintiffs' refusal-to-deal and essential facilities claims but upheld its price-squeezing claim. *Covad Communications v. BellSouth Corp.*, 374 F.3d 1044, 1049-52 (11th Cir. 2004).

The Eleventh Circuit readily dispatched the refusal-to-deal and essential-facilities claims. Finding that "*Trinko* now effectively makes the unilateral termination of a voluntary course of dealing a requirement for a valid refusal-to-deal claim under *Aspen*," and recognizing that *Trinko* treats interconnection agreements entered into pursuant to the 1996 Act as

compelled, the court concluded that *Trinko* barred the plaintiffs' claims since, prior to the interconnection agreement, there had been no voluntary course of dealing. *Id.* at 1049. As to plaintiffs' essential-facilities claim, the court found that, since *Trinko* "states that an essential facilities claim should be denied" "[w]here a state or federal agency is authorized to compel access to a competitor's infrastructure," *Trinko* required dismissal. *Id.* at 1050.

The Eleventh Circuit, however, declined to dismiss plaintiffs' price-squeezing claim. It did so for two reasons. First, it found that, since *Trinko* did not involve price-squeezing claims, *Trinko* did not "offer any definitive guidance." *Id.* Second, it found that, since plaintiffs' price-squeezing claim was "based on traditional antitrust standards," *id.* at 1052, and *Trinko* preserved existing antitrust standards, plaintiffs' price-squeezing claim survived. *Id.*

2. *Stein*

In *Stein v. Pacific Bell Telephone Co.*, plaintiff Stein, a consumer, sued defendant Pacific Bell, an incumbent LEC, alleging that Pacific Bell's failure to provide loop qualification information to competing DSL providers violated Section 2 of the Sherman Act. *Stein v. Pac. Bell Tel. Co.*, No. C 00-2915 SI, slip. op. at 10-11 (N.D. Cal. March 4, 2004).[13] Stein alleged that, by its conduct, Pacific Bell denied consumers a competitive choice in DSL service providers. *Id.* at 4.[14] Stein claimed that, unlike Verizon's dealings with its competitors in *Trinko*, Pacific Bell had

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[13] Notably, Stein did not allege price-squeezing.

[14] The court explained that "[a]n entity hoping to provide DSL service needs access to loop qualification information." *Id.* at 12.

voluntarily agreed to provide loop qualification information to its competitors as part of an effort to obtain regulatory approval of SBC's merger with Ameritech. *Id.* at 12. The court, however, concluded that the 1996 Act and FCC rules implementing it required Pacific Bell to provide loop qualification information. *Id.* at 13-14. Thus, the court concluded that *Trinko* governed and granted Pacific Bell's motion for summary judgment. *Id.* at 14-16.

3. *MetroNet*

In *MetroNet Servs. Corp. v. US West Communications*, 329 F.3d 986, 992 (9th Cir. 2003), *vacated sub nom.*, *Qwest Corp. v. MetroNet Servs. Corp.*, 124 S. Ct. 1144 (2004), a pre-*Trinko* case, MetroNet Services Corp. and MetroNet Telemanagement Corp. ("MetroNet") filed suit against Qwest, the owner of the local telephone network in 14 western states. In addition to their basic flat-rate business lines, Qwest sold "Centrex," a product which offered volume discounted phone line access and calling features to business with more than 20 phone lines. *Id.* MetroNet purchased Centrex from Qwest and resold it to small businesses in the Puget Sound region with 20 or fewer phone lines. *Id.* In 1997 Qwest changed the pricing structure of Centrex to require that each location receiving the discounted Centrex features have at least 21 lines. *Id.* This requirement rendered MetroNet's customers ineligible for the volume discount. *Id.* As a result, MetroNet filed suit against Qwest, alleging that its imposition of "per location pricing" violated Section 2 of the Sherman Act by illegally maintaining a monopoly over the market for small business local telephone services and by denying MetroNet access to an essential facility. *Id.* The district court granted summary judgment in favor of

Qwest. *Id.* On appeal, the Ninth Circuit reversed, concluding, among other things, that genuine issues of material fact precluded summary judgment on MetroNet's essential facilities claim and its claim that the "per location pricing" scheme constituted an illegal attempt to maintain a monopoly. *Id.* at 1006-13. In sustaining MetroNet's monopolization claim, the Ninth Circuit relied on a series of cases which held that attempts to eliminate discount resellers such as MetroNet can constitute monopolization. *Id.* at 1007.

On remand, the Ninth Circuit reversed its earlier decision and affirmed summary judgment in favor of Qwest. *MetroNet Servs. Corp. v. Qwest Corp.*, 2004 WL 2125769, at *1 (9th Cir. Sept. 24, 2004). The court first found that *Trinko* barred MetroNet's essential-facilities claim because the 1996 Act compels Qwest to share its facilities with its competitors, MetroNet included. *Id.* at *4. Thus, even though Qwest had made its facilities accessible to MetroNet on distinctly disadvantageous terms[15], the mere fact that "reasonable access to the essential facility exist[ed]" meant that MetroNet's claim failed. *Id.* The court then found that MetroNet's claim does not fall within the *Aspen* exception for refusal-to-deal claims because, unlike the defendant in *Aspen*, 1) Qwest was not forsaking short-term profits but trying to increase them and 2) Qwest had not refused to deal with MetroNet on the same terms that it dealt with consumers. *Id.* at *6-8. The court then concluded that it could not, in light of *Trinko*, expand existing antitrust standards to encompass MetroNet's claim

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[15] The court assumed for purposes of argument that "MetroNet [could] no longer profitably buy Centrex in the retail market and resell it to small businesses." *Id.*

that an attempt to eliminate discounter resellers constitutes exclusionary conduct. *Id.* at *8-11. The court found that, given the existence of a regulatory structure under state law, the benefits of prohibiting sellers from eliminating arbitrage were outweighed by the costs of additional supervision and regulation by the courts. *Id.* Thus, the court declined to expand the scope of Section 2 liability to prohibit Qwest's attempts to eliminate arbitrage by MetroNet. *Id.* at *11.

D. *Plaintiffs' Claims*

Plaintiffs' Complaint alleges conduct that arguably falls under three different categories of anticompetitive conduct: refusal to deal, denial of access to an essential facility, and price squeezing.[16]

1. Refusal to Deal

Defendants claim that Plaintiffs' refusal-to-deal claims are barred by *Trinko* because the Communications Act of 1934, 48 Stat. 1064, as amended, 47 U.S.C. § 151 et seq., and FCC rules implementing it, compel Defendants to offer their services to Plaintiffs. In response, Plaintiffs contend that *Trinko* is inapplicable because, unlike Verizon, Defendants are not being compelled to provide DSL service.[17]

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[16] As counsel for Plaintiffs acknowledged at the September 21, 2004 hearing, Plaintiffs' allegations, aside from the price-squeezing allegation (which is addressed separately below), are best construed as a refusal-to-deal claim. However, the Court will analyze the allegations as raising an essential-facilities claim simply to address that possibility.

[17] This argument is to be distinguished from the argument made by the plaintiff in *Z-Tel*. The *Z-Tel* plaintiff argued that its dealings with the defendant were not really compelled by law because the defendant had engaged in voluntary dealings with the plaintiff *prior* to the law's enactment. Plaintiffs here

In order to understand how the parties can characterize their dealings in such diametrically opposed terms, it is necessary to understand the complex web of regulations governing the provision of DSL services by incumbent LECs.

The Communications Act of 1934 defined telephone companies as "common carriers."[18] Common carriers were subject to the regulations set forth in Title II.[19] The development in the 1960s of data processing and other computer services that were provided over telephone lines presented a definitional and regulatory problem for the FCC. As a result, in 1966 the FCC initiated a series of proceedings to determine whether the providers of these services would be regulated under the 1934 Act. These proceedings culminated in a series of FCC orders that have become known as the *Computer Inquiries*. *See In re Regulatory and Policy Problems Presented by the*

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are alleging a refusal to deal from the moment Defendants entered the DSL market (mid-1998). Thus, Plaintiffs cannot claim that a voluntary course of dealings existed prior to the refusal to deal. Rather, Plaintiffs are asserting that Defendants' dealings with them have been voluntary from the start.

[18] 47 U.S.C. § 153(10) was originally Section 153(h) of the 1934 Act. Section 153(h) read:

> "Common carrier" or "carrier" means any person engaged as a common carrier for hire, interstate or foreign communication by wire or radio or in interstate or foreign radio transmission or energy, except where reference is made to common carriers not subject to this chapter: but a person engaged in radio broadcasting shall not, insofar as such person is so engaged, be deemed a common carrier.

47 U.S.C. § 153(h). The 1996 Act renumbered the definition of "common carrier" but did not amend it.

[19] 47 U.S.C. §§ 201-222.

Interdependence of Computer and Communication Services and Facilities, Final Order, 28 F.C.C. 2d 267 (1971) [*Computer I*]; *In re Amendment of Section 64.702 of the Commission's Rules and Regulations*, Final Decision, 77 F.C.C. 2d 384 (1980) [*Computer II*], *modified*, 84 F.C.C. 2d 50 (1980) [*Computer II Reconsidered Decision*], *further modified on reconsideration*, 88 F.C.C. 2d 512 (1981); *In re Amendment of Section 67.702 of the Commission's Rules and Regulations*, 104 F.C.C. 2d 958 (1986) [*Computer III*], *modified*, 2 F.C.C.R. 3035 (1987).[20]

In *Computer I*, the FCC decided that data processing would not be regulated by Title II but that hybrid services which combined data processing with telecommunications would be regulated on an ad hoc basis. *Computer I*, ¶¶ 27-33. The FCC further decided that common carriers wishing to provide data processing services would have to do so through a separate corporate subsidiary. *Id.* at ¶¶ 10-17.

In *Computer II*, the FCC abandoned the distinction between data processing and hybrid services.

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[20] For a thorough history of the *Computer Inquiries*, see Robert Cannon, *The Legacy of the Federal Communications Commission's Computer Inquiries*, 55 Fed. Comm. L. J. 167 (2003). *See also* Daniel F. Spulber & Christopher S. Yoo, *Access to Networks: Economic and Constitutional Connections*, 88 Cornell L. Rev. 885, 1005-09 (2003); Robert Cannon, *Where Internet Service Providers and Telephone Companies Compete: A Guide to the Computer Inquiries, Enhanced Service Providers and Information Service Providers*, 9 Comm. Law. Conspectus 49 (2001). For a nearly contemporaneous discussion of *Computer I* and *Computer II*, see *Computer & Communications Industry Association v. Federal Communications Commission*, 693 F.2d 198, 203-06 (D.C. Cir. 1982). For a discussion of *Computer III*, see *State of California v. Federal Communications Commission*, 905 F.2d 1217, 1223-30 (9th Cir. 1990).

Instead, the FCC drew a distinction between "basic services" and "enhanced services." Basic services were defined as "the offering of transmission capacity between two or more points suitable for a user's transmission needs and subject only to the technical parameters of fidelity or distortion criteria, or other conditioning." *Computer II*, ¶ 96. Enhanced services were defined as "any offering over the telecommunications network which is more than a basic transmission service." *Id.* at ¶ 97.[21] Having thus distinguished between basic and enhanced services, the FCC concluded that basic service providers would be subject to the 1934 Act's common carrier regulations but that enhanced service providers ("ESPs") would not be. *Id.* at ¶¶ 7, 127-132. However, the FCC reaffirmed *Computer I*'s ruling that common carriers

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[21] More precisely, the FCC defined enhanced services as those

> combin[ing] basic service with computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information, or provide the subscriber additional, different, or restructured information, or involve subscriber interaction with stored information.

Id. at ¶ 5.

47 C.F.R. Section 64.702(a) presently defines "enhanced services" as:

> [S]ervices, offered over common carrier transmission facilities used in interstate communications, which employ computer processing applications that act on the format, content, code, protocol, or other similar aspects of the subscriber's transmitted information; provide the subscriber additional, different, or restructured information; or involve subscriber interaction with stored information.

47 C.F.R. § 64.702(a). Section 64.702(a) further provides that "[e]nhanced services are not regulated under Title II of the Act." *Id.*

wishing to provide enhanced services must do so through a separate subsidiary but limited the applicability of this rule to AT&T and GTE. *Id.* at ¶¶ 215-218.[22]

In *Computer III*, the FCC scrapped the requirement that the "Bell Operating Companies" ("BOCs") create a separate subsidiary in order to provide enhanced services. *Computer III*, ¶ 3. Instead, the FCC created two non-structural requirements. *Id.* First, a BOC wishing to offer enhanced services was required to create a Comparably Efficient Interconnection ("CEI") Plan. *Id.* at ¶ 4. The CEI Plan required the BOC to provide competing ESPs with equal access to the network services the BOC used to provide its own enhanced services. *Id.* at ¶¶ 4-5. Second, a BOC was required to file and have approved an Open Network Architecture ("ONA") Plan. *Id.* at ¶ 6. The ONA Plan required the BOC to allow competing ESPs to have unbundled access to network elements. *Id.*

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[22] "On January 1, 1984, AT&T divested itself of its 22 local exchange companies – the Bell Operating Companies or 'BOCs' – as part of a settlement of the government's 1974 antitrust suit against AT&T. . . . Upon divestiture, the 22 BOCs were grouped into seven independent regional holding companies." *State of Cal. v. Fed. Communications Comm'n*, 905 F.2d 1217, 1225 (9th Cir. 1990). The FCC subsequently ruled that the BOCs were subject to the structural separation requirement set forth in *Computer II*. *In re Policy and Rules Concerning the Furnishing of Customer Premises Equip., Enhanced Servs. and Cellular Communications Servs. by the Bell Operating Companies*, 95 F.C.C. 2d 1117 (1983) [*BOC Separation Order*]. In a separate proceeding, the FCC released GTE from the structural separation requirement. *Computer II Reconsidered Decision*, 84 F.C.C. 2d at ¶ 66.

As amended by the 1996 Act, the 1934 Act reaffirmed the distinction between basic and enhanced services but devised a new terminology: "telecommunications" and "information services." The 1934 Act, as amended, defines "telecommunications" as "the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received." 47 U.S.C. § 153(43). It defines "information services" as

> the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and includes electronic publishing, but does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.

47 U.S.C. § 153(20). Thus, the distinction between basic and enhanced services, and the regulatory implications that flow from it, survived the 1996 Act.

The 1934 Act, as amended, defines "telecommunications services" as "the offering of telecommunications for a fee directly to the public, or to such classes as users as to be effectively available to the public, regardless of the facilities." 47 U.S.C. § 143(46). It defines "telecommunications carrier" as "any provider of telecommunications services. . ." 47 U.S.C. § 143(44). It further defines telecommunications carriers as "common carrier[s] . . . to the extent that [they] [are] engaged in providing telecommunication services. . . ." *Id.* Thus, since Defendants provide telecommunication services, Defendants are telecommunication carriers under the 1934 Act and thus

subject to the requirements and regulations that govern common carriers.

The most important of these requirements for purposes of this Motion are those set forth in Section 201 of the 1934 Act. Section 201(a) requires "every common carrier engaged in interstate commerce by wire or radio to furnish such communication service upon reasonable request thereof; and in accordance with the orders of the Commission. . . ." 47 U.S.C. § 201(a). Section 201(b) provides that "[a]ll charges, practices, classifications, and regulations for and in connection with such communication service shall be just and reasonable. . . ." 47 U.S.C. § 201(b).

The FCC has interpreted these regulations as applying to the provision of DSL transport services. *See, e.g., In the Matter of Review of Regulatory Requirements for Incumbent LEC Broadband Telecomm. Servs.*, 17 F.C.C.R. 27000, ¶ 18 (2002) [*Incumbent LEC Broadband*] (noting that SBC-ASI is required "to offer its interstate services under rates, terms, and conditions that are just, reasonable, and not unjustly or unreasonably discriminatory"); *In the Matter of Policy and Rules Concerning the Interstate, Interexchange Marketplace*, 16 F.C.C.R. 7418, ¶ 46 (2001) ("[W]e would view any discrimination in pricing, terms, or conditions [in the provision of DSL transport services] that favor one competitive enhanced service provider over another or the carrier, itself, to be an unreasonable practice under section 201(b) of the Act.").

The significance of the above-mentioned regulations and requirements to the instant case is this: As a BOC, SBC was subject to the non-structural requirements set forth in *Computer III*. Thus, when it first began offering DSL services, SBC was

required to provide competing ESPs nondiscriminatory access to the network services that it used to provide DSL. Sections 201 imposed the same requirement on SBC as a common carrier. Moreover, when SBC transitioned the provisioning of DSL transport services to SBC-ASI, SBC-ASI was subject to the same requirements.[23] *See Incumbent LEC Broadband*, ¶ 18 (noting that ASI is "obligat[ed] under our Computer Inquiry rules to offer ISPs nondiscriminatory access to the transmission capabilities underlying SBC's Internet access services."). Thus, it seems clear that, as Defendants contend, Defendants are required under the 1934 Act and FCC regulations implementing it to provide access to its DSL transport services on a nondiscriminatory basis.

Plaintiffs nonetheless assert that Defendants are voluntarily dealing with them. How can they make this claim? Essentially, Plaintiffs' argument boils down to this: that since none of the above-mentioned requirements and regulations would apply if Defendants had not voluntarily entered the DSL market, Defendants' dealings with Plaintiffs are ultimately the result of Defendants' *choice* to enter the DSL market. However, this distinction does not survive *Trinko*. Section 251(c)(3) – the provision at issue in *Trinko* – imposed on incumbent LECs a "duty to provide . . . *nondiscriminatory* access to network elements on an unbundled basis. . . ." 47 U.S.C. § 251(c)(3) (emphasis added). Thus, *Trinko* dictates that a duty to provide nondiscriminatory access is equivalent to a duty to provide access. Moreover,

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[23] Defendants contend that SBC-ASI is not a BOC but admit that 1) SBC-ASI would be subject to the requirements imposed by Section 201 in any event and 2) the FCC has treated it as a BOC.

purely as a matter of common sense and everyday language, a law that says one must do B if one does A is compulsory even if it leaves open the option of not doing A. After all, we do not describe speed-limit laws as "voluntary" simply because we have the option of not driving. Thus, while Plaintiffs' argument is not quite the "play on words" Defendants characterize it as, it ultimately fails. Consequently, this Court finds that, given the compulsory nature of Defendants' dealings with Plaintiffs, Plaintiffs' refusal-to-deal claim does not fall within the limited exception set forth in *Aspen* and is thus barred by *Trinko*.

2. Essential Facilities

Under the "essential facilities" doctrine, liability may be imposed "when one firm, which controls an essential facility, denies a second firm reasonable access to a product or service that the second firm must obtain to compete with the first." *Alaska Airlines, Inc. v. United Airlines, Inc.*, 948 P.2d 536, 542 (9th Cir. 1991). Four elements are necessary to an essential facilities claim:

> (1) control of the essential facility by a monopolist; (2) a competitor's inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasability of providing the facility.

MCI Communications Corp. v. American Tel. & Tel. Co., 708 F.2d 1081, 1132-33 (7th Cir.), *cert. denied*, 464 U.S. 891 (1983).

Absent *Trinko*, Plaintiffs' claim, if construed as an essential-facilities claim, would likely survive a motion to dismiss. The Complaint alleges facts that, if proven, would satisfy the four elements. However,

as the Eleventh Circuit indicated in *Covad*, *Trinko* requires the dismissal of an essential facilities claim "[w]here a state or federal agency is authorized to compel access to a competitor's infrastructure. . . ." *Id.* at 1050. Thus, since Defendants are required to provide access to its DSL transport services on a nondiscriminatory basis, Plaintiffs' essential facilities claim fails.

3. Price Squeeze

Plaintiffs argue that *Trinko* does not apply to their price squeeze allegations because *Trinko* did not involve a price squeeze claim. Defendants contend that the Court's reasoning in *Trinko* is equally applicable to price squeeze claims because a price squeeze claim does not differ in any relevant respect from a refusal-to-deal claim. Additionally, Defendants argue that price squeeze liability is inappropriate where, as here, wholesale prices are regulated by a federal regulatory agency.

Plaintiffs are correct that *Trinko* does not directly govern the disposition of their price squeeze allegations. *Trinko* simply does not involve price-squeeze claims. Thus, it is not directly on point. Nonetheless, Defendants contend that *Trinko* implicitly forecloses price-squeeze claims in the context of a regulated telecommunications company because a price-squeeze claim is essentially a refusal-to-deal claim. What Defendants mean by this is that a price-squeeze claim essentially boils down to a claim that Firm One is refusing to deal with Firm Two on Firm Two's price terms. This argument has a certain logic to it, and the fears that prompt it are not without

some legitimacy.[24] However, Defendants' attempt to conflate price squeeze and refusal-to-deal claims does not hold up to sustained scrutiny. While refusal-to-deal claims can arise in a wide set circumstances, price-squeeze claims can arise only in a very specific set of circumstances. As one court has explained:

> A firm can engage in a price squeeze only if it operates both as a retailer and a wholesaler whose customers are also its competitors. A price squeeze occurs when that firm's price as a wholesaler is too high or as a retailer is too low for the competitor to stay in business.

CTC Communications Corp. v. Bell Atl. Corp., 77 F. Supp. 2d 124, 142 (D. Me. 1999); *see also Town of Norwood v. New England Power Co.*, 202 F.3d 408, 418 (1st Cir.), *cert. denied*, 531 U.S. 818 (2000) ("[T]he traditional price squeeze involves a defendant who as monopolist supplies the plaintiff at one level (e.g., wholesale), competes at another (e.g., retail), and seeks to destroy the plaintiff by holding up the wholesale price to the plaintiff while depressing the retail price to common customers."). Thus, it simply is not the case that refusal-to-deal claims can always be reframed as price-squeeze claims. Moreover, to the extent that price-squeeze claims are subject to the requirements set forth in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), then the transmutability of refusal-to-deal claims is limited still more.

More compelling is Defendants' argument that price squeeze liability is inappropriate where, as

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[24] Defendants' fear that, unless *Trinko* encompasses price squeezing claims, plaintiffs can simply recast their refusal-to-deal or essential-facilities claims as price-squeezing claims.

here, wholesale prices are regulated by a federal regulatory agency. As Defendants note, the Court in *Trinko* found that the "existence of a regulatory structure designed to deter and remedy anticompetitive harm" weighed against expanding the scope of Section 2 liability. *Trinko*, 124 S. Ct. at 881. The Court explained that "[w]here such a structure exists, the additional benefit provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny." *Id.* Thus, just as the existence of a regulatory structure weighed against recognizing Trinko's refusal-to-deal claim, Defendants contend that the existence of a regulatory structure here weighs against recognizing Plaintiff's price-squeeze claims.

Though compelling, Defendants' argument has already been rejected by the Ninth Circuit. In *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992), the Ninth Circuit rejected the argument that the existence of a regulatory structure precludes antitrust liability under a price squeeze theory. While the First Circuit had previously concluded that "a price squeeze in a fully regulated industry . . . will not normally constitute 'exclusionary conduct' under Sherman Act § 2," *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 28 (1st Cir. 1990), *cert. denied*, 499 U.S. 931 (1991)[25], the Ninth Circuit deemed the First Circuit's approach "too restrictive."

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[25] Note the word "normally." The First Circuit was careful to "limit[] [its] holding by stating that 'normally' a price squeeze will not constitute an exclusionary practice in the context of a fully regulated monopoly, thereby leaving cases involving exceptional circumstances for another day." *Id.* at 29. Defendants propose no such limiting principle or language.

City of Anaheim, 955 F.2d at 1378. Instead, in *The City of Anaheim*, the Ninth Circuit imposed on plaintiffs alleging a price squeeze in a regulated industry the burden of proving that the defendant acted with specific intent. *Id.* at 1378. Thus, price-squeezing claims in the context of fully regulated industries are not foreclosed in the Ninth Circuit. This Court is bound by that precedent.[26]

Moreover, to the extent that price-squeeze claims are cognizable under existing antitrust standards[27], the policy-based arguments put forward by Defendants are misplaced. In *Trinko*, the Court first decided whether Trinko's complaint stated a viable

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[26] Even if this Court were not bound by *City of Anaheim*, however, Plaintiffs' price-squeeze claim would not necessarily be barred by *Trinko*. The reason compulsory dealings are fatal to refusal-to-deal claims under *Trinko* is because no inference of anticompetitive intent can arise where a defendant's refusal to deal was not preceded by a course of voluntary dealings. There is simply no baseline against which to judge the defendant's conduct. However, unless the prices are set by a regulatory agency, an inference of anticompetitive intent *can* be drawn from the prices charged by a defendant even where the defendant's dealings with the plaintiff are otherwise compelled by law. Moreover, Defendants overstate the implications of *Trinko*: as explained above, not even in the refusal-to-deal context does *Trinko* necessarily bar Section 2 liability in a fully regulated industry.

[27] *See, e.g., City of Anaheim v. S. Cal. Edison Co.*, 955 F.2d 1373 (9th Cir. 1992); *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802 (3d Cir. 1984); *Borough of Landsdale v. Philadelphia Elec. Co.*, 692 F.2d 307 (3d Cir. 1982); *City of Kirkwood v. Union Elec. Co.*, 671 F.2d 1173 (8th Cir. 1982), *cert. denied*, 459 U.S. 1170 (1983); *City of Groton v. Conn. Light & Power Co.*, 662 F.2d 921 (2d Cir. 1981); *City of Mishawaka v. Am. Elec. Power Co.*, 616 F.2d 976 (7th Cir. 1980), *cert. denied*, 449 U.S. 1096 (1981); *United States v. Aluminum Co. Of Am.*, 148 F.2d 416 (2d Cir. 1945).

refusal-to-deal claim under existing antitrust standards. It did so by consulting its refusal-to-deal case law: it compared Trinko's claim with the plaintiff's claim in *Aspen*. Only after it concluded that Trinko's complaint failed to state a refusal-to-deal claim under *Aspen* did the Court consult "traditional antitrust principles" in order to determine whether those principles "justif[ied] *adding* [Trinko's claim] to the few exceptions from the proposition that there is no duty to aid competitors." *Trinko*, 124 S. Ct. at 881 (emphasis added). Thus, while the *Trinko* Court justified its decision not to expand the scope of Section 2 liability by reference to the existence of a regulatory structure designed to deter and remedy anticompetitive conduct, it justified its conclusion that Trinko's allegations failed to state a claim under existing antitrust standards by reference to existing case law. Consequently, the Court's reasoning for not expanding Section 2 liability does not apply where an antitrust claim is already cognizable under existing antitrust standards. And here, unlike the plaintiff's refusal-to-deal claim in *Trinko*, Plaintiffs' price-squeezing claim falls within the range of recognized Section 2 claims.[28] Thus, the *Trinko* Court's argument against expanding the scope of Section 2 liability does not apply.

IV. CONCLUSION

Since the 1934 Act and the rules implementing it require Defendants to provide nondiscriminatory

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[28] This is not to say, however, that Plaintiffs state a viable price-squeeze claim. The parties will have the opportunity to address the viability, apart from *Trinko*, of Plaintiffs' price-squeeze claim in subsequent motions. Here, the Court is merely addressing whether *Trinko* preclude Plaintiffs' price-squeezing claim.

access to their DSL transport services, *Trinko* bars Plaintiffs' refusal-to-deal and essential-facilities claims. However, because a price-squeeze claim is actionable under existing antitrust standards, and because the Ninth Circuit has upheld the viability of price-squeeze claims in the context of highly regulated industries, *Trinko* does not bar Plaintiffs' price-squeezing claim. Thus, Defendants' Motion for Judgment on the Pleadings [16] is GRANTED IN PART and DENIED IN PART.

Further, because Plaintiff's price-squeeze claim survives this Order, and because Defendants have raised objections to the legal sufficiency of Plaintiffs' price-squeeze claim which do not derive from *Trinko*, the Court ORDERS Plaintiffs to file with the Court an amended complaint limited to the price-squeeze claim that details beyond the normal requirements of Rule 8 specific facts supporting Plaintiffs' price-squeeze claim.

IT IS SO ORDERED.

Dated: 10/19/04 /s/ STEPHEN V. WILSON
STEPHEN V. WILSON
UNITED STATES DISTRICT JUDGE

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 05-80033

D.C. No. CV-03-05265-SVW
Central California (Los Angeles)

SBC CALIFORNIA, INC., ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

[Filed July 18, 2005]

ORDER

Before: RAWLINSON and BYBEE, Circuit Judges

The petition for permission to appeal pursuant to 28 U.S.C. § 1292(b) is granted. Within 10 days of this order, petitioners shall perfect the appeal pursuant to Federal Rule of Appellate Procedure 5(d).

OPPOSITION BRIEF

77

No. 07-512

FILED
DEC 17 2007
OFFICE OF THE CLERK
SUPREME COURT, U.S.

IN THE

Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY D/B/A AT&T CALIFORNIA, *et al.*,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

I. Whether petitioners have presented compelling reason to grant the Petition seeking review of the Ninth Circuit decision affirming a district court's denial of motions to dismiss and for judgment on the pleadings on a claim alleging that a vertically integrated monopolist was liable under Section 2 of the Sherman Act (15 U.S.C. § 2) for engaging in a "prize squeeze" by charging competitors wholesale prices that are too high in relation to its unregulated retail prices charged to end-use customers – and for a period charging wholesale prices exceeding retail prices – so as to effectively preclude competition at retail.

II. Whether petitioners have shown the Ninth Circuit decision conflicts with a decision of this Court or a Court of Appeals, is contrary to any important antitrust principles articulated by this Court, or presents any issue of significant practical impact or doctrinal importance that has not been settled and demands intervention by this Court.

CORPORATE DISCLOSURE STATEMENTS PURSUANT TO SUPREME COURT RULE 29.6

Respondent linkLine Communications, Inc., has no corporate parent and no publicly held corporation owns more than 10% of its stock.

Respondent Nitelog, Inc., has no corporate parent and no publicly held corporation owns more than 10% of its stock.

Respondent In-Reach Internet, LLC (now known as InReach Internet, Inc.,) has a corporate parent named MobilePro Corp., a publicly held corporation; and In-Reach Internet, LLC, has assigned to its former corporate parent Balco Holdings, Inc., a California corporation, its rights with respect to this litigation subject to retention by MobilePro Corp. of consent and rights to receive a portion of any proceeds from this litigation as set forth in that assignment agreement dated as of October 31, 2005, by and among In-Reach Internet, LLC, InReach Internet, Inc., Balco Holdings Inc; and no publicly held corporation owns more than 10% of the stock of Balco Holdings, Inc., but MobilePro Corp. is a public held corporation that owns, and is the corporate parent of, InReach Internet, Inc., the successor of the original named Plaintiff In-Reach Internet, LLC.

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INTRODUCTION

Respondents (plaintiffs below) allege in their price squeeze monopolization claims that petitioners (defendants below), a vertically integrated monopoly, intentionally charged their retail DSL competitors, the independent ISPs (Internet Service Providers) such as respondents, wholesale prices that were too high in relation to what petitioners were charging their retail DSL customers — and for a period wholesale prices exceeded retail prices — making it impossible for independent ISPs to compete with petitioners at retail, thus assuring preservation of their monopoly. The Ninth Circuit correctly decided that *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) ("*Trinko*"), does not bar such price squeeze claims. *linkLine Communications, Inc. v. SBC California, Inc.*, 503 F.3d 876, 880-84 (9th Cir. 2007). There is no compelling reason for Petitioners' Writ of Certiorari to be granted.

The Ninth Circuit's ruling – that respondents' price squeeze claims are different from, and satisfy "established antitrust standards" independent of, a *Trinko* claim of a monopolist's "insufficient assistance" to rivals – neither contradicts *Trinko* nor creates a circuit court conflict. "*Trinko* did not involve a price squeezing theory" and "[it] took great care to explain that in this particular regulatory context, 'claims that satisfy established antitrust standards' are preserved." *linkLine*, 503 F.3d at 883 (citation omitted). "Because a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." *Id.*

The Ninth Circuit's reference to price squeeze being part of "traditional antitrust law" was based on a substantial body of pre-*Trinko* circuit court authority recognizing price squeeze allegations as stating valid claims under § 2 of the Sherman Act (15 U.S.C. § 2) against monopolists in regulated industries. *Id.* at 880.[1] And its holding that such price squeeze claims survive *Trinko* accords with *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004) ("*BellSouth*"), *cert. denied*, 544 U.S. 904 (2005). There, addressing price squeeze allegations "substantially similar" to those here,[2] the Eleventh Circuit held "[plaintiff's] price squeezing claim survives because it is based on traditional antitrust doctrine and is not specifically barred by *Trinko*," and indeed *Trinko* "'preserves claims that satisfy existing antitrust standards.'" *Id.* at 1050, 1052 (quoting *Trinko*, 540 U.S. at 407).

Petitioners incorrectly contend a circuit court split is created by the D.C. Circuit's opinion in *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005) ("*Bell Atlantic*"). That opinion held that

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1. The Ninth Circuit cited these supporting cases, *inter alia*: *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373, 1377 (9th Cir. 1992); *City of Mishawaka v. American Electric Power Co.*, 616 F.2d 976, 983-85 (7th Cir. 1980); *City of Kirkwood v. Union Electric Co.*, 671 F.2d 1173, 1178-79 (8th Cir. 1982); *Borough of Lansdale v. Philadelphia Electric Co.*, 692 F.2d 307, 309-10 (3d Cir. 1982); *City of Groton v. Connecticut Light & Power Co.*, 662 F.2d 921 (2d Cir. 1981).

2. Petitioner's Appendix ("Pet. App.") 49a n.16 (District Court Order (filed Apr. 1, 2005)).

the price squeeze claim there – alleging too high wholesale prices for the provisioning of unbundled loops compelled by new duties imposed under the Telecommunications Act of 1996 – was barred by *Trinko*. *Id.* at 673. Yet, as the D.C. Circuit explained in its order on denial of rehearing on that decision, the argument that "the court's holding 'eliminates' the antitrust claim of a price squeeze, simply misreads our opinion." *Covad Communications Co. v. Bell Atlantic Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005). "Notably, the court did not face a circumstance similar to that in *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050-52 (2004), in which the Eleventh Circuit held a claim for predatory pricing of loops could proceed; in that case the complaint alleged the 'basic prerequisites for . . . price predation.'" *Id.*

Respondents' price squeeze claims – being substantially similar to those approved by the Eleventh Circuit in *BellSouth* – would similarly survive under that D.C. Circuit's own reading of its opinion in *Bell Atlantic*. Respondents have argued that their price squeeze claims need not satisfy the predatory pricing requirements of *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). The Ninth Circuit's opinion in *linkLine* does not specifically discuss the applicability of *Brooke Group* requirements in holding that respondents' price squeeze claims could proceed. Nevertheless, as the district court below ruled in denying petitioners' motion to dismiss, "even if the *Brooke Group* requirements were applied, the [First Amended Complaint] would satisfy those requirements," noting it "contains price squeeze allegations substantially similar to those approved by the [Eleventh Circuit] in

[*Covad v. BellSouth*]." Pet. App. 48a-49a & n.16; *see id.* at 52a (*quoting* First Amended Complaint ("FAC") ¶ 26(b)); *see linkLine*, 503 F.3d at 879 (setting forth respondents' price squeeze allegations).

Neither petitioners nor Judge Gould's dissent below address that ruling of the district court nor assail the substantial similarity of the price squeeze allegations here to those approved by the Eleventh Circuit in *BellSouth* and that were distinguished by, and would survive under, the D.C. Circuit's decision in *Bell Atlantic*. Hence, there is no circuit court conflict arising from the Ninth Circuit decision affirming the district court order denying the motions to dismiss the price squeeze claims alleged here.

Further, the Ninth Circuit's recognition of respondents' price squeeze claims as an independent basis for liability under Section 2 would not deter legitimate procompetitive pricing conduct, harm consumers or conflict with any regulatory regime designed to address the antitrust harm alleged here. Respondents' price squeeze claims challenge ***unregulated*** exclusionary pricing conduct that harms competition (not merely competitors) and consumers. Monopolist-petitioners' setting of ***unregulated*** retail prices for a bundled package of DSL service, Internet access, and equipment (modem) that are lower than the wholesale input cost charged to independent ISPs for DSL service is not procompetitive price-cutting. Instead, it entails the exclusionary and purposeful elimination of retail DSL competition (monopolization), thereby depriving consumers of lower prices and choice. Pet. App. 48a-49a, 52a (district court quoting FAC ¶¶ 25(A)(1)-(3), 26(b)).

Such price squeezing is not akin to a mere failure to render sufficient assistance to rivals as alleged in *Trinko*. Rather, it amounts to a refusal to provide competitors the same services or prices otherwise made available to petitioners' retail customers – "reveal[ing] a distinctly anticompetitive bent" that distinguishes it from *Trinko* and places it within the exception to the general "no duty to deal" rule carved out by *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), and *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), as was endorsed in *Trinko*, 540 U.S. at 409.[3]

Further, imposing antitrust liability for such price squeezing would not undermine or override any regulatory regime or structure designed to deter or remedy its anticompetitive harm. *Trinko*, 540 U.S. at 411-12 (citing *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 22 (1st Cir. 1990) (Breyer, C.J.)). "*Trinko* did not . . . completely eliminate the viability of a § 2 price squeeze theory in regulated industries." *linkLine*, 503 F.3d at 883. "Moreover, the existence of regulation does not always eliminate the danger of anticompetitive harm." *Id.* "The key, under *Trinko*, is the nature of the regulatory structure at issue." *Id.* (quoting *Trinko*, 540 U.S. at 412). And here – unlike *Trinko* and *Town of Concord* – the challenged conduct does not arise in the context of a fully regulated industry. Rather there has

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3. *See MetroNet Services Corp. u Qwest Corp.*, 383 F.3d 1124, 1132-33 (9th Cir. 2004) (distinguishing *Aspen Skiing* because, unlike the defendant in *Aspen Skiing*, defendant "Qwest has been willing to sell and has sold Centrex [a business phone service] to [plaintiff] MetroNet at its retail price" and "has sold it to MetroNet on the same terms that it sells to direct consumers"), *cert. denied*, 544 U.S. 1049 (2005).

been "no comparable regulatory attention paid to t retail DSL market" and hence any "restrictions pricing at the retail level derive primarily from t antitrust laws." *Id.* at 885; *see also Town of Conco* 915 F.2d at 29 ("stress[ing]" that reasoning underlyi its holding – "'normally' a price squeeze will n constitute an exclusionary practice in the context o fully regulated monopoly" such as in the electrici industry – "applies with full force only when t monopolist who engages in the squeeze is regulated both industry levels").[4]

Finally, imposing antitrust liability for pri squeezing – where, as here, the monopolist refuses provide its competitors service at prices charged to ret customers – does not raise "concern about t administrability of a judicial remedy" because the "cou can simply order the defendant to deal with competitors on the same terms that it already deals wi others in the existing retail market, without setting t terms of dealing." *MetroNet Services Corp. v. Qwe* , 383 F.3d 1124, 1133 (9th Cir. 2004), *cert. deni* .S. 1049 (2005); *see Town of Concord*, 915 F.2d 28 (noting price squeeze allegations involving "wholes prices that *exceeded* retail prices" as "there

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4. As stated in *Town of Concord*:

> We recognize that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first. *See* [3 P. Areeda & D. Turner, *Antitrust Law* ¶ 726e, at 217-20 (1978)].

915 F.2d at 29.

eliminating some of the 'adminstrative' problems we have found surrounding a jury's efforts to determine the reasonableness of the price 'gap'" (emphasis in original)).

STATEMENT OF THE CASE

1. Background Regarding Parties, Industry and Relevant Markets

Respondents are four Internet Service Providers (ISPs). *linkLine*, 503 F.3d at 877. They provide Internet access, including via DSL service, and related services to their end user customers. *Id.* Unlike facilities-based local telephone companies, however, respondents do not own or control the transmission lines to connect their customers to the Internet; instead, they require access to petitioners' local phone facilities for such connections. *Id.*

Petitioner Pacific Bell Telephone Company or "PacBell" (now doing business as AT&T (formerly SBC California)) operates as an Incumbent Local Exchange Carrier ("ILEC"), providing local telephone services to California consumers within its local service area. *Id.* at 877-88. SBC is a subsidiary of SBC Communications, Inc. *Id.* at 878. On September 17, 1998, SBC received approval from the California Public Utilities Commission ("CPUC") to provide DSL services to California consumers. Pet. App. 27a

Petitioner Pacific Bell Internet Services ("PBIS") is a subsidiary of SBC which sold DSL Internet access to retail customers using SBC's telephone lines. *Id.* Consumers who ordered SBC's DSL and chose PBIS as

their ISP were billed the associated fee for Internet access on their regular monthly Pac Bell telephone billing statement under the heading "Pacific Bell Internet Services." *Id.*

Petitioner SBC Advanced Solutions, Inc. ("SBC-ASI") is a subsidiary of SBC Communications, Inc., and an affiliate of SBC. *Id.* In June 2000, SBC transferred responsibility for the provisioning and billing of DSL to SBC-ASI and the CPUC granted SBC-ASI a certificate of public convenience and necessity to operate as a facilities-based provider of competitive local exchange and intraLATA interexchange services. *Id.* at 27a-28a. SBC-ASI has since provided DSL and other advanced services to independent ISPs (such as respondents) and California consumers. *Id.* Petitioner SBC entities thus were organized so that they sold both wholesale transport DSL access ("DSL transport service") to independent ISPs (such as respondents) as well as retail DSL (through PBIS and then SBC-ASI) to individual consumers.

Respondents allege that the market for DSL service in SBC's telecommunication service region in California is a relevant market. (FAC ¶ 11.) DSL is distinguishable from other means of connecting to the Internet because it is (a) faster, (b) "always on," (c) more reliable, and (d) allows many users in the same geographic area simultaneous access without affecting the speed or quality of the transmission. (*Id.*) DSL is also distinguishable in that it can be made available over existing telephone lines which today connect virtually all businesses and households in California. (*Id.*) There is a discrete and separate market for DSL because of its

distinct characteristics, pricing points and separate and distinct customer demand.[5] (*Id.*)

For decades, local telephone companies (SBC, formerly PacBell) have owned and controlled facilities that are essential to the provision of many telecommunications services, including DSL service. Pet. App. 29a. In most cases, the ILEC (here SBC) owns and controls the connections to all or substantially all end user customers. *Id.* ISPs (such as respondents) that are not affiliated with the ILEC must obtain access to those customers' connections in order to reach and serve their own end user customers. *Id.* Additionally, such nonaffiliated providers often need to interconnect their own facilities with those of the ILEC if they are to be able to provide communication services on a broad scale. *Id.* Because of the critical nature of the telephone companies' network facilities, they are often referred to as "essential" or "bottleneck" facilities. This is especially true of the "last-mile" connection between the incumbent local telephone company's (SBC) central offices and the end users' premises. *Id.*

2. Respondents' Monopolization-by-Price Squeeze Claims

Because SBC is an ISP (PBIS and then SBC-ASI) and because SBC/SBC-ASI own and control the essential or bottleneck facilities for providing DSL, ISPs like respondents are in direct competition at retail with their wholesale supplier of DSL services upon which they

5. Another relevant market in this case is the market for Internet services in SBC's California service region. (FAC ¶ 12.) A third relevant market is switched local exchange telecommunications service in SBC's California service region. (*Id.*)

depend to provide DSL service. Pet. App. 29a. While there are some locations where ISPs have a choice of DSL providers, this is rare, because the majority of such wholesale DSL providers have ceased to operate in any significant geographical region of California, and SBC-ASI enjoys virtually exclusive control over DSL transport in SBC's service area (which covers approximately 78% of the geographic area of California). *Id.*

Moreover, because the SBC petitioners offer DSL services in both wholesale and retail markets, they determine the cost of the essential components of these competitor ISPs' service offerings. *Id.* at 29a-30a. Petitioners' retail affiliates, which bundle retail DSL access with both online Internet services and equipment (*e.g.*, free modem) as a package retail price to end use customers, have taken in excess of 80% of the retail DSL market. *Id.* at 30a.

Where as here the monopolists' wholesale prices are set too high relative to its low retail prices – and for a period petitioners' wholesale DSL prices to ISPs exceeded petitioners' retail prices charged end users for providing a bundle package of DSL access, Internet service and necessary equipment (*e.g.*, modem and installation) – independent ISPs are put in a price squeeze that makes it impossible to compete with the SBC petitioners in the retail market for DSL Internet service. (FAC ¶¶ 20, 25(A).) That price squeeze enabled petitioners to maintain their DSL monopoly. As respondents' amended price squeeze claims allege:

> (1) . . . [D]efendants unlawfully manipulated their dual role as vertically integrated

monopolists as both a wholesale-monopoly supplier and retail competitor of Plaintiffs by engaging in an unlawful price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which [D]efendants were providing retail DSL services and necessary equipment to end-user customers – and for a period by charging wholesale DSL prices to competing ISPs (such as [P]laintiffs) that actually exceeded the prices at which [D]efendants retail affiliate (PBIS) was charging retail end-user customers for DSL services and necessary equipment – thereby making it impossible for independent ISP competitors such as plaintiffs to compete at the low retail prices set by [D]efendants for combined DSL-Internet Service and necessary equipment provided to end-user customers.

(2) If [P]laintiffs charged retail DSL-Internet access customers the same retail price as [D]efendants' retail affiliate charged, [P]laintiffs could not cover the cost of providing DSL service, which costs necessarily includes the wholesale transport costs charged by [D]efendants.

(3) By the same token, if [D]efendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as [P]laintiffs), [D]efendants could not cover their wholesale costs and make a profit

> from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation), that were in some cases, and for some period, even below the wholesale DSL transport cost. Given the price margin relationship between retail and wholesale prices, [D]efendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as [P]laintiffs that are both wholesale customers and retail rivals.

Pet. App. 30a-31a (quoting FAC ¶ 25(A)(1)-(3) (brackets in original)); *linkLine*, 503 F.3d at 879.

Respondents further allege petitioners engaged in additional anticompetitive acts directed at independent ISPs – including anticompetitive provisioning procedures, service disruptions, disparagement, misrepresentations and improper billing – that demonstrate petitioners intended to monopolize through that price squeeze. *linkLine*, 503 F.3d at 879-80.[6]

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6. The district court granted petitioners' motion to strike the "additional anticompetitive acts" allegations, ruling that they were relevant only to the previously dismissed "refusal to deal" claims, and irrelevant to the price squeeze claims. Pet. App. 33a-36a. It rejected respondents' argument that these "additional anticompetitive acts" were probative of the requirement – imposed in cases alleging price squeeze in a regulated industry – that plaintiff must prove specific intent to monopolize by "the actions of the utility, taken as a whole." *City of Anaheim*, 955 F.2d at 1378 (citing *City of Mishawaka*).

3. District Court Rulings and Ninth Circuit Opinion

The district court denied petitioners' motions to dismiss these price squeeze claims, determining they were, unlike *Trinko's* refusal to deal claim, cognizable under existing antitrust standards and fell within the range of recognized Sherman Act Section 2 claims even in the context of a regulated (here partially regulated) industry. Pet. App. 54a-55a, 88a-90a.

The district court also addressed petitioners' motion to dismiss respondents' price squeeze claim for failure to allege the requirements of price predation under *Brooke Group*, 509 U.S. at 222-24. Pet. App. 36a-52a. The district court denied that motion, ruling "even if the *Brooke Group* requirements were applied, the [First Amended Complaint] would satisfy those requirements," noting it "contains price squeeze allegations substantially similar to those approved by the [Eleventh Circuit] in [*BellSouth*]." Pet. App. 48a-49a & n.16.

The Ninth Circuit affirmed the district court's orders denying the motions to dismiss and for judgment on the pleadings. *linkLine*, 503 F.3d at 885. The court ruled: "Based on the record before us at this time, we are able to conclude that the district court was correct to deny the SBC Entities' motion for judgment on the pleadings because linkLine's allegation that the pricing scheme created an anticompetitive price squeeze states a potentially valid claim under § 2 of the Sherman Act." *Id.*

REASONS FOR DENYING THE PETITION

Petitioners can state no compelling reasons for granting the Petition. To summarize, taking petitioners' stated grounds in order:

First, the Ninth Circuit decision – denying a motion to dismiss respondents price squeeze claims because they were viable under traditional antitrust law – does not create a circuit court conflict. The decisions of the only two other circuit courts (the Eleventh and D.C. Circuit) having addressed price squeeze claims in light of *Trinko*, have recognized the viability of predatory price squeeze claims of the type alleged here.

Second, the Ninth Circuit decision does not conflict with *Trinko*. Indeed, the price squeeze claim alleged here – involving a predatory refusal to deal with competitors on the same terms as for retail customers – falls within *Trinko*'s delineation of the exception in which a monopolist's refusal to deal gives rise to antitrust liability.

Third, petitioner cannot establish here that the Ninth Circuit decision endorses a doctrinal deviation from traditional Sherman Act principles that demands intervention by this Court – any more than was the case when review was denied of the Eleventh Circuit's decision in *BellSouth*. The Ninth Circuit's standard for imposing price squeeze liability rests on sound and settled antitrust law. Criticisms as to the purported vagueness of, or administrative problems in applying, terms used in early statements of the elements of those price squeeze claims – such as "fair price" and

"living profit"[7] – are not implicated in cases as here where, the unregulated retail prices are below the monopolist's own wholesale costs for providing service. *See Town of Concord*, 915 F.2d at 28-29. Indeed, "a special problem" seemingly perfectly suited for antitrust intervention "is posed by a [price squeezing] monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." *Id.* at 29; *see also Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 482-83 (1992) (ruling a triable issue of fact exists on Section 2 claim alleging defendant used its control over one market to gain dominance in another market).

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7. These terms were used in Judge Hand's seminal formulation of the price squeeze elements in *United States v. Aluminum Co. of America*, 148 F.2d 416, 437 (1st Cir. 1945). Though citing this case, neither the district court nor the Ninth Circuit purported to apply these terms in recognizing respondents' claims here satisfied existing antitrust standards for stating a claim of monopolization through price squeezing. As recognized in *Town of Concord*, where as here wholesale prices exceed retail prices it "eliminate[s] some of the 'administrative' problems" of applying these terms and the determining the related "reasonableness of the price 'gap'" between wholesale and retail prices. 915 F.2d at 28.

I. THE DECISION BELOW DOES NOT CONFLICT WITH PRIOR CIRCUIT PRECEDENT OR WITH *TRINKO*

A. The Ninth Circuit Decision Does Not Conflict with the Prior Decisions of the Eleventh Circuit, the D.C. Circuit or the Law of Other Circuits or *Trinko*

1. The Ninth Circuit decision allowing respondents' claims to proceed accords with the Eleventh Circuit's decision in *BellSouth*, holding that the "[plaintiffs'] price squeezing claim survives because it is based on traditional antitrust doctrine and is not specifically barred by *Trinko*." 374 F.3d at 1050. *BellSouth* noted that the *Trinko* Court "'preserves claims that satisfy existing antitrust standards'" in rejecting the argument that *Trinko* or the federal telecommunication regulation excluded facially valid price squeezing claims. *Id.* at 1052 (quoting *Trinko*, 540 U.S. at 407).

The Eleventh Circuit determined in *BellSouth* that the plaintiffs' price squeezing claim must and did "contain allegations that the two basic prerequisites for a showing of price predation under § 2 of the Sherman Act have been met" – that is, (a) "'the prices complained of are below an appropriate measure of its rival's costs'" and (b) "'a dangerous probability'" of recouping "'its investment in below-cost prices.'" *Id.* at 1050-51 (quoting *Brooke Group*, 509 U.S. at 222, 224). Respondents have satisfied that burden here.[8]

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8. Respondents have argued below, and contend, their price squeeze claims need not satisfy the predatory pricing requirements of *Brooke Group*. Nothing in the well-established (Cont'd)

The Ninth Circuit decision did not specifically discuss the applicability of *Brooke Group* requirements in its decision affirming the district court's denial of petitioners' motion to dismiss on respondents' price squeeze allegations based on the record before it. *linkLine*, 503 F.3d at 885. The record before the Ninth Circuit included the price squeeze allegations in the First Amended Complaint ("FAC"). *Id.* at 879. And as the district court ruled, in denying petitioners' motion to dismiss based on *Brooke Group*, "even if the *Brooke Group* requirements were applied, the FAC would satisfy those requirements," noting that it "contains price squeeze allegations substantially similar to those approved by the [Eleventh Circuit] in [*BellSouth*]." Pet. App. 48a-49a & n.16; *see id.* at 52a (quoting FAC ¶ 26(b)); *see linkLine*, 503 F.3d at 879 (setting forth respondents' price squeeze allegations).

In *BellSouth*, where as here the plaintiff argued it need not assert a predatory pricing claim to state a valid

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(Cont'd)
body of price squeeze authority supports this conflation of price squeeze and predatory pricing claims, particularly where wholesale prices exceed retail prices. There is no reason to apply predatory (below-cost) pricing requirements to such price squeeze claims here any more than there would be to apply them to a "practical refusal to deal" where the monopolist offers to deal with competitors "only on unreasonable terms and conditions" and refuses to "deal with its competitors on the same terms that it already deals with others in the existing retail market." *MetroNet*, 383 F.3d at 1132-33. For those situations, there should be no additional requirement that the retail prices were below cost; indeed, to the contrary, *Trinko* underscores that in *Aspen* the refusal to sell "at its own retail price" suggested a "willingness to forsake short-term profits to achieve an anticompetitive end." 540 U.S. at 409.

price squeeze claim, the Eleventh Circuit held that the allegations, substantially similar to those here, satisfied the *Brooke Group* requirements of "below-cost pricing" and "dangerous probability of recoup[ment]." 374 F.3d at 1050-52. On the below-cost pricing requirement, the court in *BellSouth* relied upon the allegations, substantively identical to those here, that:

> '[BellSouth's] retail prices for combined DSL and Internet access service are set so low relative to its unbundled wholesale loop prices that Covad cannot meet BellSouth's . . . retail prices and still make a reasonable return on its investment. If Covad charged retail DSL/ Internet access customers the same price as BellSouth does, . . . Covad could not recover the cost of providing the service, e.g., loop costs, collocation costs, transport costs, corporate overhead and sales and market costs.'

Id. at 1050; *compare with* FAC (¶ 25(A)(1) & (2) (quoted at Pet. App. 48a). After quoting these allegations, the court in *BellSouth* stated:

> Whether the last sentence in this passage reflects 'an appropriate measure of [BellSouth's] costs,' *Brooke Group*, 509 U.S. at 222, 113 S.Ct. 2578, is a factual matter for the district court to determine at a later stage of proceedings. For purposes of the pleading stage, Covad's complaint meets the first *Brooke Group* prerequisite for a showing of price predation.

BellSouth, 374 F.2d at 1051 (brackets in original).

The court in *BellSouth* then – after noting that it was alleged there (as here) that wholesale prices charged to the competitor were higher than prices charged to retail customers for combined DSL and Internet access service – stated:

> If it is true that . . . the retail prices it is charging individual customers for combined DSL and Internet service, are 'below an appropriate measure of [BellSouth's] costs,' that fact suffices to satisfy the first prong of a price predation offense under § 2 of the Sherman Act. As noted above, whether the unbundled wholesale loop prices BellSouth charges Covad pursuant to the interconnection agreement are the 'appropriate measure of [BellSouth's] costs' is a matter for the trier of fact to determine.

Id. at 1051-52 (citation omitted; brackets in original).

Here, similarly, respondents' price squeeze claim alleges that petitioners' retail prices charged to individual retail customers, for a bundle of DSL access, Internet service and necessary equipment (modem and installation), were set below its wholesale DSL transport costs petitioners charged respondents who competed at retail with petitioners' affiliates. *linkLine*, 503 F.3d at 879 (quoting price squeeze allegations of FAC). Hence, as alleged by respondents, "'if defendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as plaintiffs),'" petitioners' retail affiliates could not cover their costs at their low retail

prices for their bundled offering of DSL, Internet service, and necessary equipment – which were "'in some cases, and for some period, even below the wholesale DSL transport cost.'" *Id.* (quoting FAC). As in *BellSouth*, the district court below ruled such allegations were sufficient at the pleading stage to satisfy the "below-cost pricing" requirement of *Brooke Group*. Pet. App. 50a-51a.

On the element of recoupment, *BellSouth* relied upon the following allegations that:

> 'If BellSouth had charged itself the same wholesale price for loops, BellSouth could not make a profit from its DSL service at current prices . . . As the costs are presently allocated, BellSouth must necessarily realize a significantly higher profit margin on its wholesale sales (for which it faces no competition) than it does on the corresponding retail sales (for which Covad is attempting to compete). BellSouth intended this artificial cost allocation to harm Covad, and it did.'

374 F.3d at 1051. The *BellSouth* court held that these allegations, which are substantially similar to those set forth in respondents' FAC (¶ 25(A)(3)):

> suggest that BellSouth is compensating for deliberately reduced profits on the retail end of its operations with correspondingly greater profits on the wholesale side, in order to stifle competition from firms such as Covad that are both wholesale customers and retail rivals. We

> find that these allegations are sufficient to allege 'a dangerous probability' that BellSouth will 'recoup[] its investment in below-cost prices.' *Brooke Group*, 509 U.S. at 224, 113 S. Ct. 2578.

374 F.3d at 1051. The court then added that:

> Whether the facts contained in Covad's complaint and in the record will bear out [this] recoupment allegation against BellSouth is also a matter for the district court to determine at a later stage, not on the basis of a motion to dismiss for failure to state a claim. Taken together, Covad's price predation allegations meet the 'exceedingly low' threshold of sufficiency that a complaint must meet to survive a 12(b)(6) motion.

Id.

Here too substantially similar allegations in respondents' First Amended Complaint satisfy the recoupment standard as applied in *BellSouth* and hence survive a motion to dismiss on the pleadings. Further, as the district court determined, the complaint allegations here go beyond those found sufficient in *BellSouth* to satisfy the "dangerous probability of recoupment" requirement:

> [T]he FAC elsewhere alleges something akin to a dangerous probability of recoupment within the meaning of *Brooke Group*... [alleging] that, as a result of Defendants' anti-competitive conduct, 'competition in the provision of Internet

> services has been effectively eliminated in defendants' California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products.'

Pet. App. 51a-52a (citation omitted).

Therefore, the Ninth Circuit decision affirming the district court's denial of the motion to dismiss these price squeeze allegations here accords with the Eleventh Circuit's *BellSouth* decision; and those allegations would satisfy the antitrust standards for stating a valid price squeeze claim as set forth in that decision.

2. Petitioners incorrectly contend a "square circuit-court conflict" is created by the D.C. Circuit's opinion in *Bell Atlantic*. That opinion held that the price squeeze claim alleging an ILEC's too high wholesale prices for the provisioning of unbundled loops – a provisioning that was the purely product of "statutory compulsion" – was indistinguishable from and barred by *Trinko*. 398 F.3d at 673.

Petitioners misread this decision as an unqualified rejection of price squeeze claims where the monopolist has no duty to deal absent statutory compulsion. As the D.C. Circuit explained in its order on denial of rehearing on that decision, the suggestion that "the court's holding 'eliminates' the antitrust claim of a price squeeze, simply misreads our opinion." *Bell Atlantic*, 407 F.3d at 1222. "Notably, the court did not face a circumstance similar to that in *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050-52 (2004), in which the Eleventh

Circuit held a claim for predatory pricing of loops could proceed; in that case the complaint alleged the 'basic prerequisites for . . . price predation.'" *Id.*

It cannot be disputed here that the price squeeze claim in *BellSouth* involved the pricing for the provisioning of wholesale unbundled loops that was compelled by statute (the 1996 Federal Telecommunications Act), just as was the case in *Bell Atlantic.* Nor can it be disputed that the price squeeze allegations that were regarded by the Eleventh and D.C. Circuits as having "alleged the 'basic prerequisites for . . . price predation'" are substantially identical to those that have been alleged here.

Hence, the price squeeze claim the Ninth Circuit allowed to proceed here would not have been dismissed based on the D.C. Circuit's own interpretation of its opinion in *Bell Atlantic*, reconciling that decision with the Eleventh Circuit's allowing price squeeze claims to proceed on the basis of allegations that are legally indistinguishable from those here.

3. Further, *Bell Atlantic* is, like *Trinko*, distinguishable from this case. In *Bell Atlantic*, the monopolization claims involved access to (pricing of) unbundled loops which was "purely a creature of the 1996 [Telecommunications] Act." 398 F.3d at 673. As *Trinko* underscored in distinguishing *Aspen Skiing* and *Otter Tail*, such "unbundled elements" (as loops) were "not otherwise marketed or available to the public." *Trinko*, 540 U.S. at 410.[9] Instead, the "sharing obligation imposed

9. "In *Aspen Skiing*, what the defendant refused to provide to its competitor was a product that it already sold at retail. . . ." (Cont'd)

by the 1996 Act created 'something brand new' – 'the wholesale market for leasing network elements'" to competitors at cost-based rates, so that "Verizon's reluctance to interconnect at the cost-based rate of compensation available under [the Act] tells us nothing about dreams of monopoly." *Id.* at 410, 409 (citation omitted). Indeed, "[t]he unbundled elements offered pursuant to [the Act] exist only deep within the bowels of Verizon; they are brought out on compulsion of the 1996 Act ***and offered not to consumers but to rivals, and at considerable expense and effort.***" *Id.* at 410 (emphasis added). Hence, the Court in *Trinko* concluded "Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents." *Id.*

By contrast, here – like *Aspen Skiing* and *Otter Tail*, but unlike *Trinko* and *Bell Atlantic* – the DSL Internet service at issue is "otherwise marketed or available to the public" and petitioners here, as in *Aspen Skiing* and *Otter Tail*, are refusing to provide competitors the same services or prices made available to their retail customers, instead charging wholesale prices exceeding retail prices. *See Trinko*, 540 U. S. at 409-10 ("In *Aspen Skiing*, the defendant turned down a proposal to sell [to competitor] at its own retail price, suggesting a calculation that its future monopoly retail price would

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(Cont'd)

Trinko, 540 U.S. at 410. "Similarly, in *Otter Tail* . . . , the defendant was already in the business of providing a service to certain customers (power transmission over its network), and refused to provide the same service to certain other customers." *Id.*

be higher" and "reveal[ing] a distinctly anticompetitive bent"; and "[i]n the present case, by contrast [to *Otter Tail*], the services allegedly withheld are not otherwise marketed or available to the public."). *See also MetroNet*, 383 F.3d at 1132.

Hence, petitioners' price squeezing conduct, charging rivals higher prices than otherwise available to consumers, falls within the exception to the general "no duty to deal" rule carved out by *Aspen Skiing* and *Otter Tail*, as applied by this Court in *Trinko*.

4. Petitioners cite two pre-*Trinko* decision, *Cavalier Telephone, LLC v. Verizon Virginia, Inc.*, 330 F.3d 176, 181, 190 (4th Cir. 2003), and *Goldwasser v. Ameritech Corp.*, 222 F.3d 390, 395 (7th Cir. 2000), dismissing antitrust claims based on violations of duties arising solely from the Telecommunications Act of 1996. These decisions do not discuss whether the plaintiffs there even contended their pricing claim allegations independently satisfied existing antitrust standards. From the cryptic nature of the claims alleged in those cases it is highly doubtful they contained allegations similar to those regarded as sufficient to state valid § 2 price squeeze claims in the post-*Trinko* decisions of the Ninth, D.C. and Eleventh Circuits as discussed above. Hence, no circuit court split arises from the pre-*Trinko* decisions.

B. The Ninth Circuit Decision Does Not Threaten to Undermine *Trinko*

The Ninth Circuit decision does not assail the reasoning or result in *Trinko*. The price squeeze claims here are fundamentally different than from those

addressed in *Trinko* and "'satisfy established antitrust standards'" and so are preserved under the reasoning of *Trinko*. *linkLine*, 503 F.3d at 883 (quoting *Trinko*, 540 U.S. at 406); *see BellSouth*, 374 F.3d at 1053. Taking petitioners' contentions in turn:

1. Respondents' price squeeze claims are not, as petitioners assert, "logically or legally indistinguishable" from the "insufficient assistance" claims rejected in *Trinko*. Rather, this challenged price squeezing conduct is akin to, and reveal the same "distinctly anticompetitive bent" as, the refusals to sell to competitors at retail prices for services "otherwise marketed or available to the public" that fall within the exception to the general "no duty to deal" rule carved out by *Aspen Skiing* and *Otter Tail*, as applied by this Court in *Trinko*.

Similarly, the recognition of such price squeezing claims does not impinge on any legitimate element of a "free-market system" or chill legitimate economic growth or innovation, as discussed in *Trinko;* nor does it force an upstream monopolist to uneconomically prop up less efficient downstream rivals to the detriment of consumer welfare. The price squeeze claim here alleges an upstream monopolist engaged in exclusionary conduct aimed at dominating an unregulated retail market with the expectation that "its future monopoly retail price would be higher." *Trinko*, 540 U.S. at 409; *see Town of Concord*, 915 F.2d at 29 (recognizing the "special problem . . . posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level"). That claim does not risk putting upward pressure of retail prices, as petitioners suggest. Rather, by assuring parity of treatment between upstream monopolists'

competitors and customers, it preserves and promotes robust retail competition from equally or more efficient competitors, resulting in lower retail prices and greater choice to consumers.

Nor does redressing such price squeezing conduct impermissibly impose administratively unwieldy "day-to-day" supervisory duties on antitrust courts, as was the case in *Trinko* with respect to alleged anticompetitive violations of the regulatory sharing requirements of the Telecommunications Act of 1996. *Trinko*, 540 U.S. at 415. Unlike "[e]ffective remediation of violations of regulatory sharing requirements [that] will ordinarily require continuing supervision of a highly detailed decree," redressing price squeezing alleged here does not involve such "continuing supervision," any more than would be entailed in an addressing below-cost predatory pricing schemes. *Id.* And, as evidenced by the long line of case cited by the Ninth Circuit below, courts have been regarded as providing necessary and effective stewardship of the antitrust function in addressing anticompetitive price squeezing, even in the context of regulated industries.

Indeed, courts are particularly needed and suited to redress such price squeezing where as here "[a]ny restrictions on pricing at the retail level derive primarily from the antitrust laws." *linkLine*, 503 F.3d at 885. Further, imposing liability for plainly anticompetitive and exclusionary price squeezing of the type alleged here – involving the wholesale rates exceeding retail rates – does not raise concern about the "administrability of a judicial remedy" because "[t]he court can simply order the defendant to deal with its competitors on the same

terms that it already deals with others in the existing retail market, without setting the terms of dealing." *MetroNet*, 383 F.3d at 1133; *see Town of Concord*, 915 F.2d at 28 (noting price squeeze allegations involving "wholesale prices that *exceeded* retail prices" as "thereby eliminating some of the 'adminstrative' problems we have found surrounding a jury's efforts to determine the reasonableness of the price 'gap'" (emphasis in original)).

2. Petitioners contend that *Trinko* mandates dismissal of the price squeeze based on petitioners' insupportable assertion that any conceivable threat to competition posed by the price squeeze could be remedied by regulatory oversight. Petitioners misread *Trinko*, and the cases it relies upon, and overstate the regulatory oversight here. As the Ninth Circuit properly ruled, "*Trinko* did not . . . completely eliminate the viability of a § 2 price squeeze theory in regulated industries." *linkLine*, 503 F.3d at 883. Rather, *Trinko*, having determined that the plaintiffs' "insufficient assistance" claims would not make a "recognized antitrust claim under this Court's existing refusal-to-deal precedents," looked to whether "traditional antitrust principles justify adding the present case to the few existing exceptions from the proposition that there is no duty to aid competitors." 540 U.S. at 410-11. In doing so, it stated that "[o]ne factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm." *Id.* at 412. Hence, "the Court did not say that the existence of a regulatory scheme was a per se bar to judicial enforcement of the antitrust laws, only that 'the existence of a regulatory structure [designed to deter and remedy anticompetitive harm]'" is "'one factor' to

consider in determining whether antitrust liability might also lie." *linkLine*, 503 F.3d at 882-83 (quoting *Trinko*, 540 U.S. at 412).

Indeed, with reference to the "implied immunity" doctrine discussed in *Trinko*, it is recognized that "[a]n implied immunity may be found only where there is 'a convincing showing of clear repugnancy between the antitrust laws and the regulatory system.'" *Phonetele, Inc. v. AT&T Co.*, 664 F.2d 716, 726 (9th Cir. 1981) (Kennedy, J.) (citation omitted). And even then, an exemption will be implied "'only to the minimum extent necessary'" in order "'to make the regulatory Act work.'" *Id.* at 730 n.37 (citation omitted). Further, "the mere existence of a [regulatory] remedy within the Act does not indicate a congressional intent to displace the antitrust laws." *Id.* at 735. This is true even though the remedial scheme under the Act involved "different substantive standards." *Id.* at 734 n.46. It is well established that the "freedom of a party injured by anticompetitive conduct to elect between an administrative [Federal Communications Act] remedy and a judicial cause of action under the Clayton Act is quite acceptable; the latter need not derogate or interfere with the former." *Id.*

Moreover, "the existence of regulation does not always eliminate the danger of anticompetitive harm." *linkLine*, 503 F.3d at 883. "The key, under *Trinko*, is the nature of the regulatory structure at issue." *Id.* (quoting *Trinko*, 540 U.S. at 412). Significantly, here, unlike *Trinko* and *Town of Concord*, the challenged conduct does not arise in the context of a fully regulated industry. Rather there has been "no comparable regulatory attention paid to the retail DSL market" and hence any "restrictions on pricing at the retail

level derive primarily from the antitrust laws." *Id.* at 885; *see also Town of Concord*, 915 F.2d at 29 (recognizing the "special problem" posed by a price squeezing "monopolist, regulated at only one level, who seeks to dominate a second, unregulated level").

Petitioners refer to the FCC's decision not to subject Internet service to the "common-carrier regulation" duties imposed on ILECs for their provision of transmission facilities used to provide DSL service. *See National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967, 976, 993-94 (2005). Yet nothing in that determination suggests, much less establishes, that a "regulatory structure" exists "to deter and remedy anticompetitive harm" (*Trinko*, 540 U.S. at 412) of the type alleged here; nor does it discredit the Ninth Circuit's ruling that "[a]ny restrictions on pricing at the retail [DSL] level derive primarily from the antitrust laws" (*linkLine*, 503 F.3d at 885), nor demonstrate any tension, much less clear repugnancy, between the regulatory regime and the antitrust laws.

II. THE COURT SHOULD NOT REJECT THE "PRICE SQUEEZE" DOCTRINE ARTICULATED BY THE NINTH CIRCUIT

Petitioners cannot establish that the Ninth Circuit decision endorses a significant doctrinal deviation from traditional Sherman Act principles that demands intervention by this Court.

First, the Ninth Circuit's price squeeze liability standard relies on well-settled antitrust principles set forth in a substantial body of federal circuit case

authority recognizing the necessary and proper role of courts addressing price squeeze claims of the type alleged here, and their suitability to do so even in the context of a regulated monopolist. *linkLine*, 503 F.3d at 880. Recognizing the viability of the price squeeze claims alleged here accords with antitrust principles informing the approval of a similar claims addressed by the Eleventh Circuit in *BellSouth* and endorsed by the D.C. Circuit in *Bell Atlantic*.

Second, petitioners' criticism as to the difficulty in applying terms used in earlier price squeeze cases (*e.g.*, "fair price" or "living profit") does not render the antitrust courts either unable or unsuited to decide price squeeze claims, particularly in cases as here where the unregulated retail prices are set below the monopolist's own wholesale costs for providing service in order to exclude, or dominate, retail competition – and thereby raise prices and harm consumers. *See Town of Concord*, 915 F.2d at 28-29. Indeed, in such cases, a court's "practicable ability" in assessing price squeeze claims is no more difficult, and requires no more "continuing supervision," than applying pricing and costs standards for predatory pricing claims under *Brooke Group*.

Third, petitioners' attempted jettisoning of price squeeze liability is not supported by the First Circuit's decision in *Town of Concord*, which held that price squeeze allegations do "not ordinarily violate Sherman Act § 2 where the defendant's prices are regulated at both the primary and secondary levels." 915 F.2d at 22. As that court then clarified: "In so holding we *are not* saying either that the antitrust laws do not apply in this regulatory context, or that they somehow apply less stringently here than elsewhere." *Id.* (emphasis in

original). "And we have stressed that our reasoning applies with full force only when the monopolist who engages in the squeeze is regulated at both industry levels." *Id.* at 29. The court further stated: "We recognize that a special problem is posed by a [price squeezing] monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." *Id.* (citation omitted).

Such a "special problem" of anticompetitive harm as identified in *Town of Concord* would warrant antitrust court enforcement where, as here, "there is no comparable regulatory attention paid to the retail DSL market" so that "[a]ny restrictions on pricing at the retail level derive primarily from the antitrust laws." *linkLine*, 503 F.3d at 885. Further, as stated in *Town of Concord*, where the wholesale prices exceed retail prices, it "eliminate[] some of the 'administrative' problems we have found surrounding a jury's efforts to determine the reasonableness of the price 'gap.'" 915 F.2d at 28; *see also MetroNet*, 383 F.3d at 1133.

Fourth, the price squeeze doctrine relied on here does not, as petitioners suggest, seek to promote competitors at the expense of lawful competition, economic efficiency, legitimate price behavior or consumer welfare. Rather, it seeks to redress plainly anticompetitive conduct aimed at excluding retail competition (vanquishing equally or more efficient competition) in order to thereby monopolize, raise prices and deprive consumers of choice. *See Trinko*, 540 U.S. at 409-10 (in *Aspen Skiing*, defendant's refusal to sell to competitor at the same retail price it charged other

customers "suggest[ed] a calculation that its future monopoly retail price would be higher" and "revealed a distinctly anticompetitive bent"); *see also Eastman Kodak*, 504 U.S. at 482-83 (Section 2 claim may exist where defendant engaged in exclusionary conduct using control over one market to gain dominance in another market).

Recognizing liability for such exclusionary conduct aimed at domination of an unregulated retail market is not based on any discredited theory of "monopoly leveraging" (using monopoly to gain an competitive advantage in a second market short of attempted monopolization); nor does it condemn lawful price competition. Rather it is grounded in sound and settled antitrust principles directed at redressing anticompetitive conduct that enables the possession and exercise of monopoly power to the detriment of competition-consumer welfare that the antitrust laws were enacted to protect.

Petitioners' ruminations (based on disputed factual assertions) as to the possible (hypothetical) benefits of vertical integration cannot, on this motion to dismiss on the pleadings, trump or foreclose factual allegations of the type raised here that have been regarded – by the district court and Ninth Circuit, and by the decisions of the Eleventh Circuit and the D.C. Circuit – as stating a valid price squeeze claim under § 2 of the Sherman Act.

CONCLUSION

The petition for writ of certiorari should be denied.

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REPLY BRIEF

(6)

No. 07-512

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IN THE
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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CORPORATE DISCLOSURE STATEMENTS

Petitioners' Statements pursuant to Rule 29.6 were set forth at page iii of the petition for a writ of certiorari, and there are no amendments to those Statements.

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"*linkLine* is the most important antitrust case that the Court could take during the Fall 2007 Term." Economists and Legal Scholars Br. 1. Respondents do not contest that the Ninth Circuit has decided a recurring and important question of antitrust law. Instead, respondents argue that the Court should deny review because: first, the Ninth Circuit decision can be reconciled with the D.C. Circuit's *Bell Atlantic* decision and the Eleventh Circuit's *BellSouth* decision; second, the decision below is consistent with *Trinko*; and, third, the Ninth Circuit properly condemned price squeezes under Section 2 as "exclusionary and purposeful elimination of . . . competition." Resp. Br. 4. These arguments are incorrect.

First, respondents' argument that there is no split ignores the panel majority's correct acknowledgement that, by allowing a price-squeeze claim to proceed in the absence of an antitrust duty to deal, it had resolved the question presented in conflict with the D.C. Circuit's decision in *Bell Atlantic*. *See* Pet. App. 10a (recognizing split with *Bell Atlantic*'s holding that price-squeeze claims do not "survive *Trinko*"). The Ninth Circuit's decision also cannot be reconciled with the Eleventh Circuit's decision in *BellSouth*, which permitted a price-related claim to proceed only because the plaintiff had (in the Eleventh Circuit's view) alleged the elements of a predatory-pricing claim under *Brooke Group* – that is, below-cost pricing at the retail level and a likelihood of recoupment. By contrast, the Ninth Circuit held that plaintiffs stated a claim under Section 2 by alleging a price *squeeze* – that is, an insufficient *margin* between upstream and downstream prices charged by a vertically integrated company – without

alleging predatory pricing and despite the absence of an antitrust duty to deal in the upstream input. It was the Ninth Circuit's refusal to require allegations of predatory pricing that led Judge Gould to dissent from the decision below. The split is real.

Second, respondents seek to reconcile the Ninth Circuit's decision with *Trinko* by claiming that petitioners had an antitrust duty to deal with respondents. Resp. Br. 5. To the contrary, as the Ninth Circuit recognized (and as the district court held), there was no such duty – that is why the court below asked "whether a price squeeze is merely another term of the deal governed by the Supreme Court's analysis in *Trinko*." Pet. App. 10a; *see also id.* at 22a (dissent agreeing with *Bell Atlantic* and "a major treatise on antitrust law that 'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal'") (citations omitted). Respondents' failure to offer any *other* basis on which to distinguish their price-squeeze claim from the allegations of inadequate assistance that were at issue in *Trinko* emphasizes the conflict with controlling authority of this Court.

Third, although respondents argue that the Ninth Circuit's price-squeeze doctrine is a bulwark against anticompetitive conduct, we maintain – joined by *amici* – that the decision below protects competitors at the expense of competition and consumer welfare, in conflict with this Court's fundamental antitrust principles. Given the uncontested importance of the issue, the Court should grant certiorari.

I. THE DECISION CONFLICTS WITH THE D.C. CIRCUIT'S *BELL ATLANTIC* DECISION AND THE DECISIONS OF OTHER COURTS OF APPEALS

The Ninth Circuit squarely ruled that – despite this Court's holding in *Trinko* – a plaintiff can state a claim under Section 2 by alleging "an anticompetitive price squeeze" even when a defendant is "under no [antitrust] duty to deal with the plaintiff." Pet. App. 9a-10a, 19a. The panel majority and the dissent recognized that the D.C. Circuit in *Bell Atlantic* had reached the opposite conclusion. *See id.* at 10a (noting that the D.C. Circuit had held that "price squeeze claims" do not "survive *Trinko*"); *id.* at 22a (dissent); *see also Covad v. Bell Atlantic*, 398 F.3d at 673; *Covad v. Bell Atlantic*, 407 F.3d at 1222 ("[t]he court, following the reasoning of *Trinko*, held . . . that a claim of price squeeze cannot lie" when there is no antitrust duty to deal). The D.C. Circuit's holding accords with the pre-*Trinko* holdings of the Fourth and Seventh Circuits, which rejected price-squeeze claims along with refusal-to-deal and essential-facility claims. *See* Pet. 13. Respondents can contest none of this.

Respondents instead seek to reconcile the panel majority's decision with *Bell Atlantic* by arguing that the D.C. Circuit did not preclude the possibility of a *predatory-pricing* claim in these circumstances. *See* Resp. Br. 3, 22-23. Respondents elaborately argue, furthermore, that the Eleventh Circuit found that allegations similar to respondents' satisfied the standard for price predation under *Brooke Group*. *See id.* at 16-22. According to respondents, because the Ninth Circuit did not "specifically discuss the

applicability of *Brooke Group*" to their allegations, there is no conflict among the circuits. *Id.* at 3.

The argument fails because the panel majority articulated a legal standard for Section 2 liability based on allegations of insufficient margin between upstream and downstream prices; the standard does not require respondents to allege (and prove) predatory pricing. The panel majority did not discuss (or, indeed, even cite) *Brooke Group* because it understood that respondents' claim was a price-*squeeze* claim, *not* a predatory-pricing claim. The Ninth Circuit expressly stated that price-squeeze claims turn on the margin between upstream and downstream prices and the impact on upstream customers that are also downstream competitors. *See* Pet. App. 8a ("[A] price squeeze occurs when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market.") (internal quotation marks omitted).

Moreover, the Ninth Circuit cited seven cases for the proposition that a price squeeze may violate Section 2 – including *Alcoa*, *City of Anaheim*, and *Bonjorno* – all of which likewise make clear that a price-squeeze claim implicates the margin between upstream and downstream prices. *See, e.g.*, *Alcoa*, 148 F.2d at 438 ("That is was unlawful to set the price of 'sheet' so low and hold the price of ingot so high, seems to us unquestionable, provided, . . . that . . . the price of ingot must be regarded as higher than a 'fair price.'"); *City of Anaheim*, 955 F.2d at 1376-77 ("The vice that a price squeeze has is that . . . , for example, if a firm has a wholesale monopoly and wishes to extend that to the retail level, where it has competition, it might raise its wholesale prices

to the point that others cannot compete with it at retail."); *Bonjorno*, 752 F.2d at 808-09. The dissent reinforces the point by stressing that the panel majority should have applied – but did not apply – the *Brooke Group* standard to judge the sufficiency of respondents' allegations. *See* Pet. App. 23a (noting that "the retail side of a price squeeze cannot be considered to create an antitrust violation if the retail pricing does not satisfy the requirements of *Brooke Group*, which set unmistakable limits on what can be considered to be predatory within the meaning of the antitrust laws"). Accordingly, the conflict with the D.C. Circuit remains: under the D.C. Circuit's standard, in the absence of an antitrust duty to deal, an allegation of price squeeze does not state a claim; in the Ninth Circuit, it does.

Furthermore, whether or not respondents' complaint would have passed muster in the Eleventh Circuit,[1] the panel majority's *legal standard* also conflicts with the legal standard applied by the Eleventh Circuit.[2] In this regard, the contrast between the courts' opinions is revealing: not only did the Eleventh Circuit (unlike the panel majority) repeatedly cite *Brooke Group*, it did *not* cite a single one of the "price squeeze" cases relied on by the panel majority

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[1] It is also irrelevant that the district court apparently thought that respondents' allegations might satisfy the *Brooke Group* standard. The dissent was clearly correct that they did not (*see* Pet. App. 23a), and, in any event, that issue does not affect the Ninth Circuit's holding that it is enough for respondents to show a price *squeeze*.

[2] For its part, the D.C. Circuit had no occasion even to address what would be required to state a claim of predatory pricing in this context. *See Covad v. Bell Atlantic*, 407 F.3d at 1222 ("Covad did not argue its claim as one of price predation and . . . we did not treat it as such.").

below. The Eleventh Circuit's use of the term "price squeezing" may be confusing, but its requirement that a plaintiff show that a defendant's retail prices were below cost and that it had a dangerous probability of recoupment is plain. *See Covad v. BellSouth*, 374 F.3d at 1050-52.[3] The Ninth Circuit's standard includes no such requirement.

The circuit conflict regarding the governing legal standard merits review. Not only will the Ninth Circuit's recognition of "price squeeze" as a basis for a claim under Section 2 govern this litigation going forward, but also, more broadly, all businesses operating in the Ninth Circuit will have to conform their conduct to the panel majority's standard on pain of potential liability. Even in the absence of a duty to deal, the Ninth Circuit held, a defendant may be held liable for deliberately eliminating competitors' profit margin. As we have discussed, and as *amici* confirm, that standard not only would prohibit conduct that may benefit competition and consumers but also creates significant uncertainty in an area of particular sensitivity to the economy – pricing. *See* Verizon/NAM Br. 18-21. The existence of conflicting legal standards threatens a pervasive and deleterious effect nationwide, and provides a "compelling reason," Resp. Br. 1, for this Court to grant review.

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[3] It is seriously misleading for respondents to suggest that this Court's denial of certiorari in *Covad v. BellSouth* calls into question the appropriateness of review here. *See* Resp. Br. 14 (noting that "review was denied of the Eleventh Circuit's decision in *BellSouth*"). It was *Covad*, not BellSouth, that sought review of the Eleventh Circuit's decision, and it did so on an issue – whether Covad could sue in federal court for breach of an interconnection agreement mandated by and approved under the Telecommunications Act of 1996 – that was unrelated to the court's ruling on Covad's Section 2 claim.

II. THE DECISION CONFLICTS WITH *TRINKO*

A. As the Ninth Circuit recognized, *Trinko* holds that "the failure by a monopolist to deal with a competitor on certain service terms when that monopolist was under no duty to deal with the plaintiff competitor absent statutory compulsion, did not state a claim under § 2 of the Sherman Act." Pet. App. 9a-10a. The Ninth Circuit's decision conflicts with *Trinko* because there is no logical difference (and should be no legal difference) between a claim of inadequate access to network facilities – at issue in *Trinko* – and a claim of too-costly access to facilities – at issue here. *See* Pet. 14-15.

Respondents argue that the decision does not conflict with *Trinko* because this case falls "within [an] exception to the general 'no duty to deal' rule" in that petitioners "refus[ed] to provide competitors the same services or prices otherwise made available to petitioners' retail customers." Resp. Br. 5.[4] Respondents' argument is no defense of the panel majority's decision; it comes closer to a confession of error. Respondents defend their price-squeeze claim by insisting on the *existence* of an antitrust duty to deal – in effect, arguing that the price squeeze here should be analyzed as a constructive refusal to deal. *See* Pet. 25 n.13. But the Ninth Circuit upheld respondents' price-squeeze claim in the acknowledged *absence* of an antitrust duty to deal in the underlying wholesale input. The Ninth Circuit's holding thus conflicts with *Trinko*.

Furthermore, as the panel majority, dissent, and district court all recognized, respondents are incor-

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[4] Respondents seek to distinguish *Bell Atlantic* on the same basis. *See* Resp. Br. 23-25.

rect in asserting that petitioners had any antitrust duty to deal. As respondents elsewhere acknowledge, petitioners sell respondents "DSL transport service," Resp. Br. 8, a wholesale service that simply provides transmission capacity. Both petitioners and respondents sell to retail customers something different – *Internet access* service, *see id.* at 10, which provides not only transmission capacity but also the necessary interfaces, computer processing, connections to networks, and other services (*e.g.*, e-mail) that allow a retail customer to use the Internet.

Respondents' complaint does not allege that petitioners refused to provide *retail* DSL Internet access to respondents. As for wholesale DSL transport, petitioners had no *antitrust* duty to provide that service to respondents at all. *See* Pet. App. 9a-10a (majority), 21a-22a (dissent). The only reason that petitioners ever provided "DSL transport" was because they were compelled to do so by FCC regulations as a condition of providing retail Internet access service. *See id.* at 77a-85a (describing regulatory context). *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), and *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), are thus inapposite. *See* Pet. App. 85a (district court: "[p]laintiffs' refusal-to-deal claim does not fall within the limited exception set forth in *Aspen* and is thus barred by *Trinko*").

B. Respondents do not dispute that the FCC had the ability to address any supposed anticompetitive threat posed by excessive DSL transport prices. Instead, they argue that this degree of regulatory oversight permits antitrust intervention under *Trinko* because retail DSL Internet access prices are unregulated, leaving room for antitrust law to place

"'restrictions on pricing at the retail level.'" Resp. Br. 29-30 (quoting Pet. App. 18a). But the restriction antitrust law places on retail prices is the prohibition on predatory pricing. The question in this context is whether antitrust law should also regulate the relationship between retail prices and wholesale prices. There is no reason for it to do so in light of regulators' authority to take retail prices into account in any regulation of wholesale prices. *See* Pet. 16-17.

C. Though respondents quote the Ninth Circuit's assertion that price-squeeze claims "satisfy established antitrust standards," Resp. Br. 1, respondents conspicuously do *not* claim that any precedent of this Court has ever recognized a price squeeze as a basis for liability under Section 2. Nor do respondents make any serious attempt to reconcile the Ninth Circuit's price-squeeze standard with this Court's precedents.

Instead, respondents repeatedly quote dicta from *Town of Concord* to suggest that the price-squeeze allegations here provide an adequate basis for antitrust scrutiny; neither argument supports the claim that the decision below is consistent with *Trinko*. *First*, they note that the First Circuit adverted to the "special problem . . . posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level." 915 F.2d at 29. As an initial matter, the court below relied on no such "regulatory avoidance" theory, and respondents do not explain how it justifies the court's decision.[5] More funda-

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[5] Even setting aside "compet[ition] with connections by cable and by satellite" (and wireless networks), Pet. App. 20a, so long as the FCC continues to require petitioners to provide wholesale DSL transport, it is not clear how petitioners could raise retail prices without losing sales.

mentally, any such theory itself conflicts with *Trinko*, which made clear that regulators, not antitrust courts, should see to the effective implementation of obligations that arise from regulation and not from antitrust law. *See* 540 U.S. at 411-15.

Second, respondents emphasize their allegation that "*for a period* wholesale prices exceeded retail prices," Resp. Br. 1 (emphasis added), and note that *Town of Concord* observed that in such a situation "some of the 'administrative' problems" attending application of price-squeeze doctrine would be attenuated, 915 F.2d at 28. But neither respondents' allegations nor the Ninth Circuit's opinion are limited to circumstances where wholesale prices exceed retail prices. More important, *Town of Concord*'s observation – which at best addresses one of the institutional-competence-based objections to price-squeeze doctrine[6] – does not address at all the unsoundness of "prohibit[ing] a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal." 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c5, at 129-30 (2d ed. 2002). Petitioners need not challenge, for present purposes, the allegation that the relationship between wholesale and retail prices made it difficult for respondents to earn a profit. What petitioners

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[6] In the complicated Internet-access marketplace, there is no reason to believe that any such wholesale-exceeds-retail benchmark will be meaningful. An Internet Service Provider may have sources of revenue that supplement the monthly service fee – advertising, sales of additional services, partnerships with other Internet businesses – such that a simple comparison between the price of DSL transport and the basic retail price says nothing about whether wholesale cost exceeds expected per-subscriber revenue. The familiar examples of free Internet access service and free e-mail service illustrate the point.

dispute is that that allegation raises any antitrust concern.

III. THE NINTH CIRCUIT'S PRICE-SQUEEZE DOCTRINE IS INCONSISTENT WITH THIS COURT'S ANTITRUST DECISIONS

Respondents do not dispute the importance of the decision below, but argue that price-squeeze doctrine helps to remedy "anticompetitive conduct" that harms "competition-consumer welfare." Resp. Br. 33. We disagree. *Amici* put the matter well: "It is not possible to advance consumer welfare with an antitrust rule that punishes a firm for failing to ensure its competitors' profitability." Economists and Legal Scholars Br. 4.

Amici and commentators agree that the pervasive effect of the Ninth Circuit's decision warrants review by this Court. *See* State Attorneys General Br. 8 ("[t]he prospect of [price-squeeze] liability inevitably will deter firms in the Ninth Circuit from undertaking perfectly legal business practices"); Joseph Angland, *Antitrust in the Supreme Court: What Lies Ahead*, the antitrust source 2 (Dec. 2007) (comment by immediate past Chair of ABA Antitrust Section: "the Court should consider the price-squeeze issues raised by . . . *linkLine*"), *available at* http://www.abanet.org/antitrust/at-source/07/12/Dec07-Angland12-17.pdf. As it did last Term in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069 (2007), this Court should bring the law in the Ninth Circuit into conformity with this Court's precedents.

CONCLUSION

The petition for a writ of certiorari should be granted.

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December 28, 2007

AMICUS CURIAE BRIEF

No. 07-512

In the Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY,
DBA AT&T CALIFORNIA, ET AL., PETITIONERS

v.

LINKLINE COMMUNICATIONS, INC., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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QUESTION PRESENTED

Whether a plaintiff states a claim under Section 2 of the Sherman Act, 15 U.S.C. 2, by alleging that the defendant—a vertically integrated retail competitor with an alleged monopoly at the wholesale level—engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete, when the defendant has no antitrust duty to provide the wholesale input to the plaintiff.

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In the Supreme Court of the United States

No. 07-512

PACIFIC BELL TELEPHONE COMPANY
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v.

LINKLINE COMMUNICATIONS, INC., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

This brief is submitted in response to the order of this Court inviting the Solicitor General to express the views of the United States. In the view of the United States, the petition for a writ of certiorari should be granted.

STATEMENT

1. Petitioners are various affiliates of a dominant regional telephone company that provides telephone and data transmission services, including digital subscriber line (DSL) Internet service, to retail consumers over its telecommunications infrastructure and facilities. Respondents are Internet service providers (ISPs) that also sell DSL service at retail, in competition with petitioners. Pet. App. 2a-3a. Because petitioners own the requisite infrastructure and facilities, including local telephone lines (*id.* at 2a-3a & n.1), respondents leased

"DSL transport" from petitioners on a wholesale basis. Consequently, petitioners supplied respondents at wholesale with a necessary input to their DSL service and also competed with respondents in providing retail DSL service to consumers. *Id.* at 2a-3a. Petitioners did not supply respondents voluntarily, but rather because federal telecommunications law required them to do so. *Id.* at 5a n.6.[1]

Respondents sued petitioners in July 2003, alleging monopolization and attempted monopolization of the regional DSL market in violation of Section 2 of the Sherman Act, 15 U.S.C. 2. Respondents alleged that petitioners had "created a price squeeze by charging [respondents] a high wholesale price in relation to the price at which [petitioners] were providing retail services," Compl. ¶ 23(a), and that this "price squeeze" placed respondents at a "serious unfair disadvantage," *id.* ¶ 19. The district court described respondents' other allegations of improper conduct by petitioners, *id.* ¶ 23(b)-(f), as "refusal to deal" and "denial of access to an essential facility." Pet. App. 77a.

2. After this Court's decision in *Verizon Communications Inc.* v. *Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), petitioners moved for judgment on the pleadings, contending that *Trinko* compelled judgment in their favor. Pet. App. 65a. In an October 19, 2004, order (2004 Order), the district court granted petitioners' motion as to respondents' refusal-to-deal and essential-facility allegations, *id.* at 77a-86a, 90a-91a, but

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[1] The district court determined that the Communications Act of 1934 and implementing rules adopted by the Federal Communications Commission obligated petitioners to offer DSL transport to respondents. Pet. App. 78a-85a, and respondents did not dispute that conclusion on appeal, *id.* at 5a n.6.

denied the motion as to the price-squeeze claim. *Id.* at 86a-91a.

The court held that *Trinko* did not "directly" bar a claim based on price-squeeze allegations, rejecting petitioners' argument that "a price squeeze claim is essentially a refusal-to-deal claim," *i.e.*, "a claim that Firm One is refusing to deal with Firm Two on Firm Two's price terms." Pet. App. 86a. Although the court acknowledged that the argument "has a certain logic to it," it rejected it on the ground that not all refusal-to-deal claims can "be reframed as price-squeeze claims." *Id.* at 87a. The court also stated that, "to the extent that price-squeeze claims are subject to the requirements set forth in *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), [for predatory-pricing claims,] then the transmutability of refusal-to-deal claims is limited still more." *Ibid.*

The district court also rejected petitioners' argument that "price squeeze liability is inappropriate where, as here, wholesale prices are regulated by a federal regulatory agency." Pet. App. 87a-88a. The court observed that *Trinko* pointed to the "existence of a regulatory structure designed to deter and remedy anticompetitive harm" as a reason not to expand the scope of Section 2 liability. *Id.* at 88a (quoting *Trinko*, 540 U.S. at 412). The court concluded that regulation of petitioners' wholesale prices was not determinative because, under governing Ninth Circuit precedent, the existence of a regulatory structure does not preclude antitrust liability for a price squeeze, *id.* at 88a-89a (citing *City of Anaheim* v. *Southern Cal. Edison Co.*, 955 F.2d 1373 (1992)), and such a claim "falls within the range of recognized Section 2 claims," *id.* at 90a. Accordingly, the court held that "*Trinko* does not bar [respondents'] price-squeezing claim." *Id.* at 91a.

The district court did not reach petitioners' "objections to the legal sufficiency of [respondents'] price-squeeze claim which [did] not derive from *Trinko*" (Pet. App. 91a), including petitioners' argument that the complaint failed to satisfy the *Brooke Group* requirements—*i.e.*, pricing below an appropriate measure of costs and a dangerous probability of recoupment. See Mem. in Supp. of J. on Pleadings 15. The court instead ordered respondents to file an amended complaint detailing the specific facts supporting their price-squeeze claim. Pet. App. 91a.

3. Respondents filed an amended complaint, and petitioners then moved to dismiss it, arguing *inter alia* that price-squeeze claims must satisfy the *Brooke Group* requirements and that the amended complaint failed to do so. Pet. App. 36a. In an April 1, 2005, order (2005 Order), the district court denied that motion. *Id.* at 25a-57a. Although the court found the "policy arguments" for applying the *Brooke Group* requirements "persuasive," *id.* at 47a, the court concluded that it was unnecessary to resolve that "difficult issue" (*ibid.*) because the amended complaint would satisfy those requirements when "generously construed" in accordance with the "no set of facts" standard of *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957). Pet. App. 49a, 56a.[2]

The court granted petitioners' alternative request to amend the 2004 Order to certify it for interlocutory appeal pursuant to 28 U.S.C. 1292(b), identifying the "controlling question of law" as "whether *Trinko* bars price squeeze claims in a fully regulated industry" in which "the parties are compelled to deal under the federal

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[2] That view of the applicable pleading requirements was subsequently repudiated by this Court in *Bell Atlantic Corp.* v. *Twombly*, 127 S. Ct. 1955, 1969 (2007).

communications laws." Pet. App. 53a, 56a-57a. The court stated that "the issue before the Ninth Circuit will not only be whether *Trinko* bars price squeeze claims generally but, more specifically, whether it bars predatory price squeeze claims (i.e., price squeeze claims which comply with the *Brooke Group* requirements)." *Id.* at 56a n.22.

4. The court of appeals granted permission to appeal, Pet. App. 92a, and a divided panel affirmed, *id.* at 1a-24a.

a. The panel majority framed the question presented as whether *Trinko* bars price-squeeze claims against a defendant "who has no duty to deal with the plaintiff absent statutory compulsion." Pet. App. 1a. The majority explained that a price squeeze occurs "when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market." *Id.* at 8a (quoting 2 Julian O. von Kalinowski et al., *Antitrust Laws and Trade Regulation* § 27.04[1], at 27-40 (2d ed. 2007)). It stated that federal courts have recognized the viability of such price-squeeze claims under the Sherman Act since *United States* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945). Pet. App. 8a-9a. The panel majority declined to reconsider, and instead reaffirmed, the Ninth Circuit's *Anaheim* decision, which held that price-squeeze claims are "viable against monopolists in regulated industries" if the plaintiff proves "specific intent on the part of the wholesale monopoly holder." *Id.* at 9a, 14a.

The majority reasoned that "*Trinko* did not * * * completely eliminate the viability of a § 2 price squeeze theory in regulated industries." Pet. App. 15a. To the contrary, the majority concluded that *Anaheim* was

"consistent with *Trinko*" in "reject[ing] the wholesale importation of antitrust theory as applicable to regulated industries." *Ibid.* The majority stated that in "any future application of *Anaheim*" the court would "ensure consistency with *Trinko*." *Id.* at 16a.

Applying *Anaheim* and *Trinko*, the court upheld the district court's denial of judgment on the pleadings. Pet. App. 16a-19a. It emphasized that the Federal Communications Commission regulates only "the wholesale prices [petitioners] charged [respondents]; there is no comparable regulatory attention paid to the retail DSL market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws." *Id.* at 18a. The court stated that it was "unclear at this juncture the extent to which [respondents are] basing [their] § 2 price squeezing theory on wholesale pricing, retail pricing, or both." *Ibid.* But, "since [respondents] could prove facts, consistent with [their] complaint, that involve only unregulated behavior at the retail level, [their] action or lawsuit survives a motion for judgment on the pleadings." *Ibid.* The court thus concluded that the price-squeeze allegation "states a potentially valid claim" under Section 2. *Id.* at 19a.

b. Judge Gould dissented, concluding that the district court should have dismissed the amended complaint in its entirety. Pet. App. 19a-24a. In his view, *Trinko* "takes the issues of wholesale pricing out of the case, and thus transforms what is left of any claim of 'price squeeze.'" *Id.* at 20a. Therefore, "the retail side of a price squeeze cannot be considered to create an antitrust violation if the retail pricing does not satisfy the requirements of *Brooke Group*." *Id.* at 23a. Respondents could state a valid claim only by alleging "market power in the retail market," as well as the *Brooke Group* requisites for a predatory-pricing claim. *Id.* at 20a-21a.

Judge Gould concluded that the amended complaint did not satisfy those standards, although he found "just enough possibility of an injury" to warrant permitting respondents a further opportunity to amend the complaint. *Id.* at 23a, 24a n.2.

DISCUSSION

Section 2 of the Sherman Act does not provide a cause of action for "price-squeeze" claims of the type at issue here—namely, allegations that a vertically integrated company with an alleged monopoly at the wholesale level, but with no antitrust duty to provide that wholesale input to its retail competitors, engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow its retail competitors to compete. Accepting such a price-squeeze theory based solely on an inadequate margin between a defendant's wholesale and retail prices would recognize an antitrust claim involving no allegations of predatory pricing, no breach of an antitrust duty to deal, and no conduct that harms competition in a way the antitrust laws forbid. Such a theory of liability could not be reconciled with this Court's modern antitrust jurisprudence. The court of appeals' contrary holding is erroneous and is in conflict with the decisions of other courts of appeals. Despite the interlocutory posture of the case, review is warranted because the Ninth Circuit's endorsement of such a theory threatens to chill retail price-cutting by vertically integrated firms and encourage litigation designed to protect competitors at the expense of competition, thereby undermining the procompetitive purposes of the antitrust laws and harming consumers. Accordingly, the petition should be granted.

A. The Decision Below Is Contrary To This Court's Modern Antitrust Jurisprudence

1. In *Verizon Communications Inc.* v. *Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), this Court held that the violation of a statutory and regulatory requirement to deal with rivals does not automatically establish a duty to deal for purposes of the antitrust laws. *Id.* at 405-407. The Court also concluded that Verizon, a dominant telecommunications company that was required by telecommunications law to provide rival companies with access to portions of its network, had no antitrust duty to assist a rival in the circumstances of that case. *Id.* at 407-416. The Court distinguished *Aspen Skiing Co.* v. *Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), which held that a particular refusal to deal with a competitor amounted to exclusionary conduct, and observed that *Aspen* "is at or near the outer boundary of § 2 liability." *Trinko*, 540 U.S. at 409.

Contrasting the allegations in *Trinko* with the facts in *Aspen*, the *Trinko* Court emphasized the absence of any allegation that Verizon "voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion." 540 U.S. at 409; cf. *Aspen*, 472 U.S. at 605-611. *Trinko* thus held that "Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents." 540 U.S. at 410. The Court further concluded that "traditional antitrust principles" did not justify expanding "the few existing exceptions from the proposition that there is no duty to aid competitors," especially given "the existence of a regulatory structure designed to deter and remedy anticompetitive harm." *Id.* at 411-412.

Here, respondents' price-squeeze allegations amount to nothing more than a claim that petitioners refused to deal on terms that respondents desired. The original complaint was based on the allegedly "high wholesale price" that petitioners charged respondents "in relation to the price at which [petitioners] were providing retail services." Compl. ¶ 23(a).[3] But as the case comes to this Court, petitioners had no antitrust duty to deal with respondents at the wholesale level (see Pet. App. 1a, 85a), and thus no *antitrust* duty to provide respondents with any particular wholesale price terms. Rather, just like the interconnection services provided by Verizon in *Trinko*, petitioners provided DSL transport to respondents only under compulsion of the telecommunications laws. *Id.* at 5a n.6, 77a-85a.[4]

From the standpoint of federal antitrust law, therefore, there would be no antitrust violation even if petitioners refused to deal with respondents altogether (and thereby barred them from the retail market entirely).

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[3] Because the district court assessed only the viability of the original complaint in the 2004 Order (which is the only order that was unambiguously certified for appeal, see pp. 17-19, *infra*), the discussion in text focuses on that complaint. The analysis would be the same if the allegations of the amended complaint were considered, because those allegations likewise turn on the allegedly insufficient margin between wholesale and retail prices. Pet. App. 5a-8a.

[4] Respondents argue in this Court that petitioners had an antitrust duty to deal cognizable under *Aspen*, based on the contention that petitioners had "refus[ed] to provide competitors the same services or prices made available to their retail customers." Br. in Opp. 24. Neither the court of appeals nor the district court addressed that argument, presumably because the complaint contains no suggestion that respondents ever sought, or desired, to purchase from petitioners the bundled Internet access service (incorporating DSL transport) that petitioners sold at retail. See Compl. ¶¶ 8, 12, 19. Accordingly, that issue is not properly presented here.

It necessarily follows that there can be no valid price-squeeze claim based merely on petitioners' conduct in charging "wholesale prices that were too high in relation to what petitioners were charging their retail DSL customers" (Br. in Opp. 1), because that conduct amounts to nothing more than a refusal to deal with respondents on advantageous terms. A defendant that has no duty to deal with rivals by definition has no duty to deal with them on particular terms that would permit them to compete.

Thus, there can be no stand-alone price-squeeze claim in this case. If respondents could state any antitrust claim arising out of petitioners' pricing, it would have to be a claim of predatory pricing based on the retail price. But the original complaint nowhere alleged that petitioners' retail prices were below an appropriate measure of petitioners' costs, nor did it allege a dangerous probability of recoupment. Accordingly, respondents' allegation that the margin between petitioners' wholesale and retail prices impeded their ability to compete (Compl. ¶¶ 19, 23(a); Br. in Opp. 1) fares no better than the similar allegations regarding the provision of inadequate wholesale services in *Trinko*.

2. The Ninth Circuit rejected the notion that "a price squeeze is merely another term of the deal governed by" *Trinko*. Pet. App. 10a. In its view, "[b]ecause a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." *Id.* at 14a. Some federal courts have "recognized price squeeze allegations as stating valid claims under the Sherman Act," *id.* at 8a-9a, beginning with *United States* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) (*Alcoa*). Like the "'essential facilities' doctrine crafted by some lower

courts," *Trinko*, 540 U.S. at 410, however, the price-squeeze theory of antitrust liability has never been recognized by this Court. In the government's view, the Ninth Circuit erred in reaffirming the viability of pure price-squeeze claims in the circumstances here. When the defendant has no antitrust duty to deal, price-squeeze allegations that are based solely on the margin between an integrated defendant's wholesale and retail prices cannot be reconciled with this Court's post-*Alcoa* antitrust jurisprudence.

As this Court's cases make clear, Section 2 does not condemn unilateral action that disadvantages a rival in the absence of anticompetitive conduct. See, *e.g.*, *Trinko*, 540 U.S. at 407 (monopolization); *Spectrum Sports, Inc.* v. *McQuillan*, 506 U.S. 447, 456-460 (1993) (attempted monopolization). Whether one competitor inflicts "painful losses" on another "is of no moment to the antitrust laws if competition is not injured," because "[i]t is axiomatic that the antitrust laws were passed for 'the protection of *competition*, not *competitors*.'" *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993) (quoting *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 320 (1962)); see *Weyerhaeuser Co.* v. *Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1077-1078 (2007). Even a firm with monopoly power has no general duty under the antitrust laws to assist its rivals. See *Trinko*, 540 U.S. at 407-409.

The price-squeeze theory reaffirmed by the court of appeals—focusing solely on the margin between a vertically integrated firm's retail price and the wholesale price at which it sells an essential input to retail competitors, Pet. App. 8a—is inconsistent with those principles. A low retail price is ordinarily benign or procompetitive because "[l]ow prices benefit consumers regardless of how those prices are set, and so long as they are above

predatory levels, they do not threaten competition." *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U.S. 328, 340 (1990). This Court has adhered to that principle "regardless of the type of antitrust claim involved." *Ibid.* A high upstream price, on the other hand, is ordinarily lawful because the "charging of monopoly prices[] is not only not unlawful; it is an important element of the free-market system." *Trinko*, 540 U.S. at 407. In most situations, moreover, mitigating a squeeze would require either substituting price regulation for the free-market price-setting mechanism ordinarily protected by the antitrust laws or requiring "firms to maintain supracompetitive prices" downstream, "thus depriving consumers of the benefits of lower prices." *Brooke Group*, 509 U.S. at 224.

Accordingly, a price squeeze does not necessarily, or even ordinarily, entail anticompetitive conduct within the meaning of the antitrust laws. As a leading antitrust treatise explains, "[m]ost" price squeezes are not "invidious." 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c at 126 (2d ed. 2002); see *ibid.* (observing that "it is difficult to see any *competitive* significance apart from the consequences of vertical integration itself, which may be adverse, neutral, or beneficial"). See also *Town of Concord* v. *Boston Edison Co.*, 915 F.2d 17, 23-25 (1st Cir. 1990) (Breyer, J.) (noting that "[m]erely eliminating competitors is not necessarily anticompetitive" and discussing "traditional circumstances in which prices that create a squeeze might simultaneously bring about economic benefits"), cert. denied, 499 U.S. 931 (1991).

Price-squeeze theories focus on the economic well-being of particular competitors, not on competition. The gravamen of the offense found in *Alcoa* was that independent sheet rollers, squeezed between the pincers of

Alcoa's high price for ingot (from which sheet is made) and the low price at which Alcoa itself sold sheet, could not make a "living profit." 148 F.2d at 437. The court deemed that result unlawful as long as the price of ingot was "higher than a 'fair price.'" *Id.* at 438. Similarly, the price-squeeze theory reaffirmed by the Ninth Circuit forbids pricing wholesale inputs so high that the defendant's "'customers cannot compete with it in the second-level'" market. Pet. App. 8a (citation omitted). In either case, what makes the conduct purportedly unlawful is its adverse effect on a competitor. See Compl. ¶ 19 (alleging that petitioners' price squeeze placed respondents at a "serious unfair disadvantage"). Under this Court's cases, however, a firm's conduct may not be judged anticompetitive, predatory, or exclusionary "by simply considering its effect on" a competitor. *Aspen*, 472 U.S. at 605.

Because a price squeeze is ordinarily not anticompetitive, a complaint whose allegations of anticompetitive conduct are limited to such a squeeze, at least when the defendant has no antitrust duty to deal, does not suffice to establish that "the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2); see *Bell Atl. Corp.* v. *Twombly*, 127 S. Ct. 1955, 1965-1966 (2007) (noting that a complaint's "[f]actual allegations must be enough to raise a right to relief above the speculative level"). The court of appeals was therefore wrong to conclude that respondents' price-squeeze allegations stated a potentially valid antitrust claim.

Rather, in this context, respondents' price-squeeze theory could not allege exclusionary conduct without at least satisfying the *Brooke Group* requirements with respect to the retail market. But then the gravamen of the complaint would no longer be a price squeeze (*i.e.*, an insufficient margin between wholesale and retail

prices) as such, but rather the predatory nature of petitioners' retail price (*i.e.*, below-cost pricing). As the dissent concluded (Pet. App. 20a-21a), for such a complaint to be viable, it would at least have to satisfy *Brooke Group* by alleging that "the prices complained of are below an appropriate measure of its rival's costs" and that the defendant had "a dangerous probability[] of recouping its investment in below-cost prices." 509 U.S. at 222-224.[5]

The panel majority adverted to the possibility that respondents "could prove facts, consistent with [their] complaint, that involve only unregulated behavior at the retail level." Pet. App. 18a. But unlike the dissenting judge, the majority did not hold or suggest that a price-squeeze complaint must contain allegations sufficient to satisfy the *Brooke Group* standard in order to survive a motion for judgment. *Id.* at 19a. The Ninth Circuit's reaffirmation (*id.* at 14a) of "price squeeze theory" as a "viable" and independent "part of the fabric of traditional antitrust law" cannot be squared with this Court's modern antitrust cases.

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[5] There may be cases in which a defendant's prices are set for exclusionary purposes, but no antitrust liability arises because the defendant has neither violated an antitrust duty to deal nor priced below cost. Indeed, this Court pointedly acknowledged in *Brooke Group*, 509 U.S. at 223, that above-cost prices may be exclusionary in effect. But whether or not such prices are the downstream component of a price squeeze, their exclusionary effect, even if not simply a reflection of one party's cost structure and therefore of competition on the merits, "is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting." *Ibid.*

B. The Decision Below Conflicts With Decisions Of Two Other Circuits

The decision of the court of appeals conflicts with the post-*Trinko* decisions of two other circuits. First, in *Covad Communications Co.* v. *BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004), cert. denied, 544 U.S. 904 (2005), the Eleventh Circuit considered antitrust claims brought by Covad, a DSL provider, against a dominant telephone company that both provided wholesale services to Covad under regulatory compulsion and competed with it in the retail DSL market. On remand from this Court for reconsideration in light of *Trinko*, the Eleventh Circuit held that Covad's price-squeeze allegations remained viable after *Trinko*—but only because (in the court's view) the complaint "contain[ed] allegations that the two basic prerequisites for a showing of price predation under § 2 of the Sherman Act have been met." *BellSouth*, 374 F.3d at 1050 (citing *Brooke Group*). Thus, the Eleventh Circuit *rejected* the viability of a traditional, stand-alone price-squeeze claim (*i.e.*, a claim based on the margin between wholesale and retail prices), and upheld only a predatory-pricing claim involving "price squeezing allegations." *Ibid.* The Ninth Circuit's description of *BellSouth* as "holding that price squeeze claims survive *Trinko*" therefore conveys an inaccurate impression. Pet. App. 10a. In contrast to the decision below, the Eleventh Circuit expressly held that to survive *Trinko* a price-squeeze complaint "*must* contain allegations * * * of price predation." *BellSouth*, 374 F.3d at 1050 (emphasis added). That amounts to a recognition that a price-squeeze claim as such, independent of allegations of predation at the retail level, is not viable after *Trinko*.

Second, as the Ninth Circuit acknowledged (Pet. App. 10a), its decision squarely conflicts with the D.C.

Circuit's decision in *Covad Communications Co.* v. *Bell Atlantic Corp.*, 398 F.3d 666 (2005), which involved similar price-squeeze allegations by Covad against a different dominant telephone company. In the wake of *Trinko*, the D.C. Circuit held that price-squeeze claims based solely on the margin between retail and wholesale prices are not viable in that context. *Id.* at 673-674. The court thus affirmed dismissal of Covad's price-squeeze claim, observing that "it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal." *Id.* at 673 (quoting 3A Areeda & Hovenkamp ¶ 767c5, at 129-130).

Subsequently, the D.C. Circuit explained in an order denying rehearing that its decision in *Bell Atlantic* was not in conflict with *BellSouth*, noting that it had not reached a claim alleging predatory pricing: "Covad did not argue its claim as one of price predation and, unsurprisingly, we did not treat it as such." *Covad Commc'ns Co.* v. *Bell Atl. Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005). Thus, both the D.C. Circuit and the Eleventh Circuit have made clear that price-squeeze allegations based solely on the margin between wholesale and retail prices, against a defendant with no antitrust duty to deal, fail to state a Section 2 claim.[6]

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[6] Although the reasoning in pre-*Trinko* decisions from the Fourth and Seventh Circuits is in tension with the decision below, and both accurately foreshadow this Court's decision in *Trinko*, neither of them expressly reaches the viability of a price-squeeze claim. See *Cavalier Tel., LLC* v. *Verizon Va., Inc.*, 330 F.3d 176 (4th Cir. 2003), cert. denied, 540 U.S. 1148 (2004); *Goldwasser* v. *Ameritech Corp.*, 222 F.3d 390 (7th Cir. 2000).

C. The Decision Below Warrants Review

1. The procedural details of the certification process are an unattractive feature of this case, but it remains an adequate vehicle for this Court's review of the important issue presented. The record in this case creates some doubt regarding the precise scope of the matters that were properly before the court of appeals on interlocutory appeal. As this Court has explained, an appeal under Section 1292(b) "is from the *certified order*, not from any other orders that may have been entered in the case," *United States* v. *Stanley*, 483 U.S. 669, 677 (1987), and therefore confers appellate jurisdiction only over that order and "any issue fairly included" within it, *Yamaha Motor Corp.* v. *Calhoun*, 516 U.S. 199, 205 (1996). Although the court of appeals looked to both the initial complaint and the amended complaint in deciding the appeal (Pet. App. 4a-8a), and stated that "[f]or purposes of this appeal, we assume as true the facts pleaded in [respondents'] amended complaint" (*id.* at 2a n.2), it is not clear that the district court certified any order besides the 2004 Order (which addressed only the original complaint). That uncertainty, however, does not affect this Court's jurisdiction to address the question presented, and accordingly it is not a basis for denying review.

In its 2005 Order granting certification, the district court stated that the standards for certification of an interlocutory appeal under 28 U.S.C. 1292(b) were satisfied, and accordingly "GRANT[ED] [petitioners'] Motion to Certify October 20, 2004, Order for Interlocutory Appeal [27]." Pet. App. 57a. The referenced motion asked the court to "certify for interlocutory review its ruling on this motion if adverse to [petitioners], and amend this Court's October 20, 2004 Order to certify for interlocutory review so much of the Order as permits

[respondents'] price-squeeze claim to proceed." Mot. to Strike, Dismiss, or Certify 1 (03-5262 Docket Entry No. 27 (C.D. Cal. Jan. 14, 2005)). By granting the referenced motion, the district court necessarily granted the request to amend the 2004 Order to certify that order for interlocutory appeal, thereby satisfying the requirement that the statutory certification prerequisites be "state[d] in writing in such order." 28 U.S.C. 1292(b); see, *e.g.*, Fed. R. App. P. 5(a)(3) ("the district court may amend its order * * * to include the required permission or statement"); *In re Hamilton*, 122 F.3d 13, 14 (7th Cir. 1997).

Petitioners' motion to certify (although styled a motion to "Certify October 20, 2004, Order") also sought certification of the district court's ruling on "this motion," *i.e.*, petitioners' alternative motion to strike or dismiss the amended complaint, to the extent the court rejected the motion. Because the district court "GRANT[ED]" the motion to certify without any explicit qualification, it could be argued that the court thereby certified (and the Ninth Circuit accepted for appeal) the court's denial of petitioners' motion to dismiss in the 2005 Order, as specifically requested in petitioners' motion to "Certify October 20, 2004, Order." That interpretation is bolstered by the district court's suggestion (Pet. App. 56a n.22) that the issues before the Ninth Circuit would include the ruling on the amended complaint, a view arguably shared by the court of appeals as well (*id.* at 2a n.2, 19a).

On the other hand, the only "controlling question of law" specifically identified by the district court as justifying interlocutory appeal was the 2004 Order's ruling on the viability of price-squeeze claims under *Trinko* (Pet. App. 53a, 56a-57a), whereas the 2005 Order addressed the sufficiency of the amended complaint under

Brooke Group (*id.* at 36a-52a). Moreover, in staying proceedings pending resolution of the interlocutory appeal, the district court referenced only the "interlocutory appeal of this Court's October 20, 2004 Order." Stip. & Order Staying Action 2.[7]

Regardless of whether the 2005 Order was properly before the court of appeals, that court did have jurisdiction to review the propriety of the 2004 Order denying petitioners' motion for judgment with respect to the original complaint. The court of appeals resolved that issue in favor of respondents, holding that price-squeeze claims remain viable after *Trinko* and that the Ninth Circuit's recognition of such claims in *Anaheim* in the context of regulated industries remains good law. Pet. App. 8a-16a. Accordingly, this Court possesses jurisdiction to review those holdings.[8]

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[7] The court of appeals was less than precise about what was before it. The court discussed both the 2004 and 2005 Orders and, in its paragraph summarizing the 2005 Order, stated that the district court certified "the order" for interlocutory appeal. Pet. App. 2a. In the end, however, it affirmed the district court's denial of petitioners' "motion for judgment on the pleadings," *id.* at 19a, which was the ruling in the 2004 Order, not the 2005 Order.

[8] The district court did not decide until the 2005 Order whether respondents' allegations satisfy the *Brooke Group* standard. Even assuming that the district court did not certify that order for interlocutory appeal, however, there would be no jurisdictional impediment to this Court's consideration of *Brooke Group* and other modern antitrust precedents in reviewing the propriety of the 2004 Order. An interlocutory appeal encompasses "any issue fairly included" within the certified order. *Yamaha*, 516 U.S. at 205. The 2004 Order denied petitioners' motion for judgment with respect to respondents' original price-squeeze claim (which plainly did *not* allege predatory pricing under *Brooke Group*), and the certification of that order therefore conferred appellate jurisdiction to review the correctness of that denial. In reviewing the 2004 Order, this Court would therefore possess jurisdiction to determine whether a stand-alone price-squeeze claim against a

2. Respondents contend (Br. in Opp. 14) that the decision below does not warrant review because the Ninth Circuit's decision accords with *Trinko* and *BellSouth* with respect to "predatory price squeeze claims of the type alleged here." Respondents are mistaken.

In the first place, respondents' contention that they have alleged a claim of "predatory" pricing is based on the allegations in the amended complaint, which the district court concluded in its 2005 Order were sufficient to satisfy the *Brooke Group* requisites if "generously construed." Pet. App. 56a. As discussed, however, it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal. Respondents do not contend, and there is no basis for suggesting, that the original complaint alleged the elements of a predatory-pricing claim under *Brooke Group*.

But more to the point, even if respondents do have a predatory-pricing claim that would satisfy *Brooke Group*, they also have a claim in the Ninth Circuit that does not require satisfaction of *Brooke Group*, and that is not a claim they would have in the Eleventh or D.C. Circuits. That is enough to provide an adequate vehicle for review. The panel majority did not address the sufficiency of respondents' allegations under *Brooke Group* or hold that price-squeeze claims must satisfy the *Brooke Group* standard in order to survive a motion to dismiss. Indeed, the majority did not even discuss the subject of "predatory" pricing at any point in its opinion,

---

defendant with no antitrust duty to deal is consistent with modern antitrust precedents (including both *Trinko* and *Brooke Group*). To be sure, the Court might lack jurisdiction to decide the distinct questions whether (a) respondents could avoid dismissal by alleging the elements of a predatory-pricing claim under *Brooke Group*, and (b) whether the amended complaint alleged such a claim, but those questions would not merit this Court's review at this time in any event.

notwithstanding the dissent's extended analysis of that issue.

To be sure, the panel majority did state that respondents might be able to "prove facts, consistent with its complaint, that involve only unregulated behavior at the retail level." Pet. App. 18a. The court did not hold that such a theory would have to satisfy the *Brooke Group* standard in order to be viable, however, nor did it foreclose alternative theories of price-squeeze liability. And the court elsewhere made clear that, in the Ninth Circuit at least, the traditional price-squeeze theory recognized in *Alcoa* and its progeny "remain[s] viable" after *Trinko*. *Id.* at 14a; see *id.* at 8a-9a, 14a-16a. Indeed, respondents endorse that reading of the court's decision, because they continue to "contend * * * [that] their price squeeze claims need not satisfy the predatory pricing requirements of *Brooke Group*." Br. in Opp. 16 n.8.

Accordingly, the majority opinion stands for the erroneous proposition that respondents' price-squeeze allegations survive *Trinko*, regardless of whether respondents also alleged the elements of a predatory-pricing claim under *Brooke Group*. The decision cannot plausibly be read to limit price-squeeze claims to the predatory-pricing context. The conflict with the D.C. and Eleventh Circuits, and with this Court's modern antitrust jurisprudence, is therefore stark.

3. Notwithstanding the interlocutory posture of the case, this Court's review is warranted to correct the Ninth Circuit's erroneous decision on an important legal issue and to resolve the conflict among the circuits. The court of appeals instructed the district court to permit respondents' price-squeeze claim to go forward, without requiring price-predation allegations, thus removing any element of exclusionary conduct from a potentially large class of monopolization and attempted monopolization

claims. The risk of large damage awards may induce settlements in such cases, and thereby deny this Court an appropriate future opportunity to correct the Ninth Circuit's error. Of even greater concern, however, the risk of treble damages may cause firms like petitioners that must offer wholesale services to hesitate to offer low-cost retail products, to the detriment of consumers and competition.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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AMICUS CURIAE BRIEF

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In The
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY,
SBC INTERNET SERVICES, INC., and
SBC ADVANCED SOLUTIONS, INC.,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC.,
INREACH INTERNET, INC.,
OM NETWORKS, and NITELOG, INC.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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QUESTION PRESENTED

When a firm is under no duty to deal under antitrust law, may a plaintiff state a claim under Section 2 of the Sherman Act by alleging that the firm engaged in a price squeeze?

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INTEREST OF AMICI

The interests of the States are twofold. First, because the States are among the leading enforcers of antitrust law, they have a compelling interest in ensuring the soundness and uniformity of antitrust jurisprudence. The lower court created a conflict among the Circuits and announced an exception to *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004). Although the States need resolution of the circuit conflict, the States also want an interpretation that is rational and predictable – a price-squeeze claim cannot be maintained against a firm that has no antitrust duty to deal. Such a bright-line rule will encourage and support competition, innovation, and growth in the marketplace for the ultimate benefit of consumers.

Second, the States have a critical interest in preserving the efficiency and the integrity of their marketplace by reducing costs associated with unfounded lawsuits. Businesses in the United States face the highest legal costs in the industrialized world.[1] Antitrust litigation imposes significant

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[1] According to the Office of Management and Budget, "[t]he costs of litigation per person in the United States are far higher than in any other major industrialized nation in the world. Lawsuit costs have risen substantially over the past several decades, and a significant part of the costs go to paying lawyers' fees and transaction costs – not to compensating the injured parties." *Promoting Economic Opportunity and Ownership*, OFF. OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, BUDGET OF THE UNITED

(Continued on following page)

burdens on firms, the courts, and society. *Trinko*, 540 U.S. at 414-15. If, as the Ninth Circuit held, an antitrust plaintiff can state a price-squeeze claim even though the defendant has no duty to deal, then businesses will face more litigation. Firms will be prompted to settle these cases, even at a high cost, to avoid even higher discovery costs and the uncertainties of litigation. These expenses will ultimately be passed on to consumers.

REASONS FOR GRANTING THE PETITION

The Petition should be granted for three reasons. First, the Ninth Circuit's decision is contrary to the interest of consumers. Second, this Court should grant review to resolve a conflict among the Circuits. Third, this Court should grant review to reaffirm the principles it announced in *Trinko*.

I. THE NINTH CIRCUIT'S DECISION UNDERMINES THE INTERESTS OF CONSUMERS.

Regarded as "the Magna Carta of free enterprise," *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 610 (1972), the Sherman Act seeks to prohibit the acquisition or maintenance of monopoly

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STATES GOVERNMENT, FISCAL YEAR 2006 (2005), available at http://www.whitehouse.gov/omb/budget/fy2006/promoting.html.

power – the power to control prices or exclude competition – by means other than growth or development as a consequence of a superior product, business acumen, or historic accident. *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966). Because a monopolist has no incentive to reduce prices, improve quality, or offer greater selection, the antitrust laws "were enacted for the protection of *competition* not *competitors*." (emphasis original) *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (internal quotations omitted). Competition ultimately benefits consumers in the form of lower prices, higher quality, and larger selection.

The Ninth Circuit's decision undermines these principles. It protects competitors – the downstream rivals who are upset by the firm's pricing policies – rather the competition of the marketplace. If a firm faces potential liability for a "price squeeze," even though it has no antitrust obligation to deal with its downstream competitors, then the firm will be reluctant to engage in competitive behavior that would prompt a lawsuit by its downstream competitors. *See* William J. Baumol & Janusz A. Ordover, *Use of Antitrust To Subvert Competition*, 28 J.L. & ECON. 247, 254 (1985). Most obviously, the firm may shy away from vertical integration. That is, it will refuse to enter the downstream market. Consumers rarely benefit when a firm refuses to enter a market. Less competitors in a market may lead to concentrations of economic power and, eventually, monopoly power. Similarly, because there is a "long

recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal," *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919), a vertically integrated firm simply may refuse to sell its upstream products to its downstream competitors. Such a development will remove any economic efficiency that would result from such sales. Production costs for downstream firms will be higher. Those higher production costs inevitably will be passed on to consumers in the form of higher prices.

Vigorous competition among firms is good for consumers, but bad for those firms that are the weakest in the marketplace. William J. Baumol & Alan S. Blinder, ECONOMICS: PRINCIPLES & POLICY 275 (10th ed. 2006). The Ninth Circuit's decision allows the weak firms to chill the behavior of strong firms to the detriment of consumers. *See Trinko*, 540 U.S. at 414. The Magna Carta of free enterprise does not mandate such a result. Certiorari should be granted.

Moreover, the Ninth Circuit's decision penalizes companies for above-cost price cutting, something this Court has been "particularly wary" of allowing recovery for "because allowing such claims could, perversely, 'chill legitimate price cutting, which directly benefits consumers.'" *Weyerhauser Co. v. Ross-Simmons Hardwood Lumber Co., Inc.*, 127 S. Ct. 1069, 1074 (2007). Consumers benefit from lower prices "regardless of how these prices are set, and so long as they are above predatory levels, they do not

threaten competition." *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990). Condemning practices resulting in lower prices to consumers is thus "especially costly" because "cutting prices in order to increase business often is the very essence of competition." *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986).[2]

Even if the Ninth Circuit's price-squeeze theory were sound, and the benefits of a price squeeze did not exist, it still should be rejected in light of the difficulty courts would have in administering the test the theory requires. *Town of Concord v. Boston Edison*, 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, J.). As then Judge, now Justice Breyer, explained the numerous difficulties:

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price

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[2] As this Court observed:

> "the purpose of the Sherman Act is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself. It does so not out of solicitude for private concerns but out of concern for the public interest.

Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993).

> without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will?

Id. at 25. These difficulties explain "why antitrust courts normally avoid direct price administration." *Id.*[3] The assumption of "day-to-day controls characteristic of a regulatory agency"[4] that the courts of appeals rationale would require disserve the goals of the antitrust laws.

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[3] *See also United States v. Trenton Potteries Co.*, 273 U.S. 392, 397 (1927) ("[t]he reasonable price fixed today may through economic and business changes become the unreasonable price of tomorrow"); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 283 (6th Cir. 1898) (stating that to inquire into the reasonableness of prices is to "set sail on a sea of doubt"), *aff'd*, 175 U.S. 211 (1899).

[4] Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 ANTITRUST L.J. 849, 853 (1989).

II. THERE IS A CONFLICT AMONG THE CIRCUITS.

As the Ninth Circuit explicitly acknowledged, *Pet. App.* at 10a, the decision below directly conflicts with the D.C. Circuit's decision in *Covad Commc'ns Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005). In *Covad*, the D.C. Circuit held that where the Sherman Act[5] did not impose a duty to deal, a plaintiff could not state a "price squeeze" claim. *Covad*, 398 F.3d at 673-74. As the D.C. Circuit recognized, "it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal." *Id.* at 673 (quoting 3A Phillip Areeda & Harold Hovenkamp, ANTITRUST LAW § 767 c.3 (2nd ed. 2002)). Although the conflict between the lower court and the D.C. Circuit is sufficient to justify this Court's review, the Ninth Circuit's decision also conflicts with decisions from the Fourth, Seventh, and Eleventh Circuits. *See Covad Commc'ns Co. v. BellSouth Corp.*, 374 F.3d 1044, 1052 (11th Cir. 2004),[6] *cert. denied*, 544 U.S. 904 (2005); *Cavalier Telephone, LLC v. Verizon Virginia, Inc.*, 330 F.3d 176, 181, 190 (4th Cir. 2003), *cert. denied*, 540 U.S. 1148 (2004); *Goldwasser v. Ameritech Corp.*, 222 F.3d 390, 395 (7th Cir. 2000).

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[5] 15 U.S.C. § 2.

[6] Although the Eleventh Circuit allowed a "price-squeeze" claim to proceed, as the petitioners note, the claim was limited "to instances that involved predatory pricing." *Covad v. BellSouth*, 374 F.3d at 1052. *See* Cert. Pet. at 13.

This conflict among the Circuits has serious consequences. In the Ninth Circuit, firms that have no statutory obligation to deal with their competitors may be subjected to antitrust litigation if a plaintiff alleges the firm engaged in a "price squeeze." In sharp contrast, similarly situated firms in the District of Columbia, Fourth, Seventh, and Eleventh Circuits do not face such litigation. The prospect of such liability inevitably will deter firms in the Ninth Circuit from undertaking perfectly legal business practices that might prompt a price-squeeze lawsuit. Resolution of conflicts among the Circuits is a principal basis for certiorari. *Braxton v. U.S.*, 500 U.S. 344, 347 (1991).

III. THE NINTH CIRCUIT'S DECISION CONTRADICTS *TRINKO*.

Even if there were no conflict among the Circuits, review by this Court would still be appropriate to reaffirm and clarify the scope of *Trinko*.

In *Trinko*, this Court held that when a monopolist has no antitrust duty to deal, there is no antitrust liability if the monopolist fails to provide "assistance in provision of service to rivals." *Trinko*, 540 U.S. at 411. As this Court explained:

> Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the purpose of antitrust law, since it may lessen

> the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion.

Id. at 407-08. In the absence of antitrust duty to deal, firms need not provide favorable services or prices to their rivals.

"Any claim for excessive rates can be couched as a claim for inadequate services and vice versa," *AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 223 (1998). Thus, the *Trinko* claim – inadequate service to rivals – logically can be characterized as a claim that excessive rates are being charged to rivals. Indeed, the D.C. Circuit recognized that the claims were the same. *Covad*, 398 F.3d at 673. Put another way, the *Trinko* claim is logically the same as a price-squeeze claim in this case. In both cases, a firm that has no antitrust obligation to deal is being sued for an antitrust violation because it refuses to give favorable terms to a competitive rival. Since the *Trinko* claim was invalid, then it logically follows that a price-squeeze claim is invalid. *Covad*, 398 F.3d at 673-74.

The Ninth Circuit ignored this logic. Because *Trinko* did not specifically involve a price-squeeze claim, the court of appeals found that price claims "remain viable notwithstanding either the telecommunications statutes or *Trinko*." *Pet. App.* at 14. Under the Ninth

Circuit's reasoning, a firm that has no duty to deal cannot be sued for failing to assist its downstream competitors, *Trinko*, 540 U.S. at 410-11, but can be sued for failing to give favorable prices to its down stream competitors. Such a distinction makes no sense. Either the firm can be sued for both or it can be sued for neither. This Court should grant review to reaffirm *Trinko* and extend its holding to the failure to give favorable prices. Certiorari should be granted.

CONCLUSION

For the reasons stated above, in the Petition itself, and in the other amici briefs supporting the Petitioners, the Petition for Certiorari should be **GRANTED.**

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AMICUS CURIAE BRIEF

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d/b/a AT&T CALIFORNIA, *et al.*,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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QUESTION PRESENTED

Whether a plaintiff states a claim under section 2 of the Sherman Act by alleging that the defendant—a vertically integrated retail competitor with an alleged monopoly at the wholesale level but no antitrust duty to provide the wholesale input to competitors—engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete.

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INTERESTS OF THE *AMICI CURIAE*

Amici are professors and scholars in law and economics who have taught, or have conducted research on, antitrust law and the economics of industrial organization.[1] They include William J. Baumol, Robert H. Bork, Robert W. Crandall, George Daly, Harold Demsetz, Jeffrey A. Eisenach, Kenneth G. Elzinga, Gerald Faulhaber, Franklin M. Fisher, Charles J. Goetz, Robert Hahn, Jerry A. Hausman, Thomas M. Jorde, Robert E. Litan, Paul W. MacAvoy, J. Gregory Sidak, Pablo T. Spiller, and Daniel F. Spulber. A summary of names and affiliations appears in the Appendix at the end of this brief. *Amici* file solely as individuals and not on behalf of any institutions with which they are affiliated.

INTRODUCTION

As professors and scholars in law and economics who teach and conduct academic research on antitrust law, we believe that *linkLine* is the most important antitrust case that the Court could take during the Fall 2007 Term.

We agree with the petitioners that the Ninth Circuit has generated an inescapable conflict among circuits, and that the Ninth Circuit's opinion below is incompatible with this Court's reasoning in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), *Weyerhaeuser Co. v. Ross-Simmons*

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[1] Neither of the parties has participated in the drafting of this brief. No person other than the *amici* made a monetary contribution to the preparation or submission of this brief.

Hardwood Lumber Co., 127 S. Ct. 1069 (2007), and *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). We agree with Judge Gould's dissent in *linkLine* that *Trinko* "takes the issues of wholesale pricing out of the case," such that the plaintiffs' only possible remaining theory of harm would be predatory pricing at the retail level—which the plaintiffs did not allege. *linkLine Commc'ns Inc. v. Pac. Bell Tel. Co. d/b/a/ AT&T Cal., Inc.*, No. 05-56023, 2007 U.S. App. LEXIS 21719, at *28-29 (9th Cir. Sept. 11, 2007) (Gould, J., dissenting). We also agree with Judge Ginsburg's opinion for the D.C. Circuit in *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005), which in turn embraces the conclusion of the Areeda-Hovenkamp treatise that "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Id.* at 673-74 (quoting 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 767c3, at 129-30 (2d ed. 2002)). The existence of a rule like *linkLine* has a pervasive impact on business behavior that, at the margin, affects competition and consumers. This deleterious effect extends beyond the telecommunications industry to affect all firms that do business in the Ninth Circuit.

These reasons justify granting certiorari in *linkLine* and reversing the Ninth Circuit's decision.

SUMMARY

In our minds, an even larger reason than those described above makes it imperative that the Court take this case. The Ninth Circuit's decision in *linkLine* implicates the normative foundation of modern Sherman Act jurisprudence: that antitrust law exists to advance consumer welfare. We have three points to make.

First, any rule of price-squeeze liability that threatens liability based on the claim that the difference between a firm's upstream and downstream prices leaves downstream rivals insufficient margin substitutes a rule of competitor welfare for consumer welfare.

Second, properly understood, a price squeeze is a regulatory issue, which makes sense only as a rule of price regulation in an industry already subject to duties to deal and to control by institutionally competent regulators. Attempting to implement regulatory policy through section 2 of the Sherman Act is ill-advised, both because it makes no sense for courts to re-regulate deregulated or lightly regulated industries, and because courts lack the institutional competence to implement regulation.

Third, the Ninth Circuit's rule is of pressing concern precisely because it will deter efficiency-enhancing conduct and competitive pricing. Vertical integration and partial integration are ubiquitous, and firms need to be able to make decisions about such integration without the threat of liability. Vertically integrated firms likewise need to be free to cut retail prices (as long as the prices are not predatory) without concern for rivals—the point

of *Brooke Group*. Moreover, the Ninth Circuit's standard is so vague and open-ended that it creates uncertainty and invites litigation; it also permits imposition of liability based on apparently subjective evaluation of disputed and hard-to-prove facts, which will lead to a substantial risk of false positives.

ARGUMENT

It is not possible to advance consumer welfare with an antitrust rule that punishes a firm for failing to ensure its competitors' profitability. If *linkLine* stands, the lower federal courts will have put antitrust at war with itself to a degree not witnessed since the years before the Court's conscious decision, three decades or more ago, to infuse antitrust law with greater economic rigor so that it might better advance consumer welfare.

The alternative to consumer-welfare maximization is the view that antitrust law is simply one more tool of industrial policy, and thus its application may permissibly compromise consumer welfare to advance the welfare of competitors. Other nations evidently consider this normative proposition to be appropriate, if recent developments in the European Union are a valid indication. More than ever before, the United States and Europe appear to be at a fork in the road over whether the law of monopolization exists to protect consumers or to ensure that a specified number of firms will profitably populate a market. The Ninth Circuit's *linkLine* decision implicitly chooses the latter path, which leads to the Potemkin village of "managed competition." *See* Robert W. Crandall & Hal J. Singer, *Life Support for Unaffiliated ISPs?*, REGULATION, Fall 2005, at 46.

To say that American antitrust law does not—and should not—recognize a cause of action for price squeeze by a firm that owes no duty to deal with rivals is not to say that one cannot find the concept of a price squeeze embraced somewhere else in American law. One can. In public utility regulation, the price-squeeze issue arises in proceedings concerning "access pricing" and "imputation."[2] Extensive economic literature exists on how regulators would maximize consumer welfare in the pricing of bottleneck inputs that a vertically integrated monopolist sells to its competitors in a downstream market. But three points about price-squeeze regulation bear emphasis.

First, these cases are highly technical *regulatory* proceedings that are typically protracted and factually intensive. *See Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, J.) (a price-squeeze case requires a court to "act[] like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years"). Price-squeeze cases are precisely the kinds of proceedings that would be unwieldy to attempt to replicate through antitrust litigation. Imputation analysis requires the estimation of incremental cost. Economic estimation of that nature demands a kind of quantitative expertise that a judge or

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[2] *See, e.g.*, WILLIAM J. BAUMOL & J. GREGORY SIDAK, TOWARD COMPETITION IN LOCAL TELEPHONY (MIT Press 1994); William J. Baumol & J. Gregory Sidak, *The Pricing of Inputs Sold to Competitors*, 11 YALE J. ON REG. 171 (1994); William J. Baumol & J. Gregory Sidak, *The Pricing of Inputs Sold to Competitors: Rejoinder and Epilogue*, 12 YALE J. ON REG. 177 (1995); Jerry A. Hausman & Timothy J. Tardiff, *Efficient Local Exchange Competition*, 40 ANTITRUST BULL. 529 (1995).

jury is not likely to possess. Even so ambitious and invasive a monopolization case as the Bell System divestiture, *United States v. AT&T Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983), did not attempt to use antitrust law as a tool for regulating the price of wholesale services supplied by monopoly local exchange carriers.

Second, these regulatory proceedings arise because the vertically integrated firm has a preexisting regulatory duty to deal with competitors in a downstream market. This feature is the element of compulsion that was so critical to the Court's reasoning in *Trinko*. *See Trinko*, 540 U.S. at 412-16.

Third, the experience with price-squeeze cases brought by national competition authorities in Europe under Article 82 of the Treaty of Rome reveals the economic and factual complexity of correctly implementing the imputation analysis in an antitrust case. It becomes necessary to hypothesize what an efficient competitor would be and then determine whether the defendant's wholesale and retail prices permit the efficient competitor to earn some level of profit deemed to be sufficient.[3] This kind of analysis,

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[3] *See, e.g.*, Michele Polo, *Price Squeeze: Lessons from the* Telecom Italia *Case*, 3 J. COMPETITION L. & ECON. 453 (2007); Laura Ferrari Bravo & Paolo Siciliani, *Exclusionary Pricing and Consumer Harm: The European Commission's Practice in the DSL Market*, 3 J. COMPETITION L. & ECON. 243 (2007); Damien Geradin & Robert O'Donoghue, *The Concurrent Application of Competition Law and Regulation: The Case of Margin Squeeze Abuses in the Telecommunications Sector*, 1 J. COMPETITION L. & ECON. 355 (2005).

however, merely underscores (1) that the primary concern in price-squeeze cases is not consumers, but competitors, and (2) that, in the American setting, the requisite analysis more resembles the work of a public utilities commission than that of a federal judge presiding over an antitrust case. By definition, the judge's job as de facto rate regulator never ends because external forces will compel wholesale and retail prices to change over time, such that a given profit margin may shrink and jeopardize the survival of competitors. The perverse outcome is that price-squeeze litigation becomes a kind of enduring cost-of-service regulation that taxes the resources of a single district judge.

The Telecommunications Act of 1996 provides an instructive analogy that provoked multiple opinions in *AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366 (1999). There, the statute (applied in a regulatory proceeding) entitled a competitor to access any one or more of an incumbent local exchange carrier's unbundled network elements at a regulated price if that competitor would be "impaired" in its ability to supply a (downstream) telecommunications service in the event that the competitor were denied access to a particular network element (at the regulated price). Congress did not attempt to provide a precise economic definition of "impairment." It is a measure of the complexity of administering that concept that Justices Scalia, Breyer, and Souter debated how much of a cost disadvantage would be enough to trigger the "impairment" standard. *Iowa Util. Bd.*, 525 U.S. at 392, 399-400, 416-18. That question admitted no easy answer—and it got none in multiple remands to the Federal Communications Commission over the course of many years. Yet the

determination of "impairment" under the Telecommunications Act fundamentally resembles the line of economic analysis that a court would need to undertake in a price-squeeze case based on the Sherman Act.

Shortly after *Iowa Utilities Board*, some scholars on telecommunications regulation argued that the "impairment" exercise should be regarded as unproductive unless it could be shown that finding "impairment" and granting a competitor access to the incumbent's bottleneck element at a regulated price would increase consumer welfare in the downstream market. *See* Jerry A. Hausman & J. Gregory Sidak, *A Consumer-Welfare Approach to Mandatory Unbundling of Telecommunications Networks*, 109 YALE L.J. 417 (1999). In other words, if there is no causal connection between assisting competitors and improving consumer welfare, then the regulatory intervention is strictly a wealth transfer. The same criticism applies to an antitrust cause of action for price squeeze. The theory of price squeeze is dissonant with consumer welfare maximization for the simple but perverse reason that, as conceived by the Ninth Circuit, harm to consumer welfare is irrelevant to the imposition of antitrust liability.

A word about *United States v. Aluminum Co. of America (Alcoa)*, 148 F.2d 416 (2d Cir. 1945), is necessary because the Ninth Circuit is incorrect to the extent that it reads *Alcoa* to have imposed section 2 liability under a price-squeeze theory for an attempt to monopolize the downstream (aluminum sheet) market. It is too abbreviated for the Ninth Circuit to characterize *Alcoa*

as "holding [Alcoa's] price squeeze unlawful," *linkLine*, 2007 U.S. App. LEXIS 21719, at *11, and then to assert that "a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko* . . . ." *Id.* at *19.

In *linkLine*, the plaintiffs argued that the telephone company used its retail pricing of DSL Internet access (aluminum sheet) and its pricing of DSL transport (aluminum ingot) to monopolize DSL Internet access (aluminum sheet). In *Alcoa*, however, the Second Circuit said that the price squeeze, which it found to deny downstream competitors a "living profit" in violation of section 2 of the Sherman Act, "was not part of an attempt to monopolize the 'sheet' market." *Alcoa*, 148 F.2d at 438. Because the analogy to sheet aluminum in *linkLine* is DSL Internet access (not DSL transport), *Alcoa* does not support the position of either the plaintiffs or the Ninth Circuit that the alleged price squeeze potentially violates section 2 *with respect to the alleged market for DSL Internet access.*

Moreover, *Alcoa*'s concern over preserving a "living profit" for Alcoa's competitors could not be farther removed from the contemporary consumer-welfare orientation of antitrust law. The Court in *Trinko* considered *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), to be on the ragged edge of viability as a theory of antitrust liability. The "living profit" reasoning of *Alcoa* should be sufficient to confirm that, sometime during the intervening 62 years, the Court's evolving jurisprudence based on consumer-welfare maximization implicitly overruled the competitor-welfare premise of *Alcoa*'s price-squeeze

analysis.[4] For example, in *Trinko* this Court said that courts should not act as "central planners." *Trinko*, 540 U.S. at 408. However, to determine a "fair price" and a "living profit," two of three elements of a prima facie price-squeeze claim under the *Alcoa* analysis, a court must do just that. Forcing a firm to share its resources with downstream competitors, and dictating "fair prices" for these resources, strains the resources of the judiciary, as this Court has noted.

In *Alcoa*, the Second Circuit asserted that the purpose of the Sherman Act is to "preserve, for its own sake and *in spite of possible cost*, an organization of industry in small units." *Alcoa*, 148 F.2d at 429 (emphasis added). All of the legal analysis in *Alcoa* that builds from this premise is suspect in light of the fact that, at least three decades ago, this Court emphatically expressed a different normative objective for antitrust law. Today, *Alcoa*'s view of the normative purpose of antitrust law more closely resembles Europe's perspective than America's. In *NCAA v. Board of Regents of the University of Oklahoma*, 468 U.S. 85 (1984), *Trinko*, and many other cases, this Court has endorsed the view that the Sherman Act's concern is consumer welfare, not competitor welfare. Compelling an income transfer from a vertically integrated firm to its downstream competitors does not advance the Sherman Act's consumer-welfare goal.

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[4] Compare, for example, how the D.C. Circuit in *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 226 (D.C. Cir. 1986) (Bork, J.), reasoned that, by 1986, certain Supreme Court decisions had been implicitly overruled by the analysis contained in the Court's more recent cases embracing the consumer-welfare approach.

In light of this weak foundation for the price-squeeze theory of liability, we find it startling that the Ninth Circuit never discussed the First Circuit's decision in *Town of Concord*, written in 1990 by then-Judge Breyer. *Town of Concord* is the single most informative opinion in American antitrust jurisprudence for understanding the law and economics relevant to evaluating a price-squeeze claim. It is no surprise that this Court's decision in *Trinko* quotes liberally from *Town of Concord* and confirms the correctness of its reasoning that the antitrust laws are concerned with the competitive *process*, not its end results. The Ninth Circuit relied on decisions from the Second, Third, Seventh, and Eighth Circuits—but its survey of the pertinent law on price squeezes did not reach Judge Breyer's extended analysis in *Town of Concord*.

In *Town of Concord*, the First Circuit rejected a price-squeeze claim for reasons that implicate the validity of *Alcoa*. First, the court noted that a price squeeze can have procompetitive effects: "the primary-level monopolist might carry out its second-level activities more efficiently than its independent competitors," thereby eliminating less efficient second-level competitors from the market, which results in lower prices and saves economic resources. 915 F.2d at 24. Moreover, if a second-level firm is itself a monopolist, it is desirable to allow the upstream monopolist to squeeze out the downstream monopolist, because the downstream monopolist, in its effort to extract its own monopoly rents, can increase the price of the end-product beyond the price that results from just one firm's extraction of monopoly rent (either realized at the wholesale or retail level). *Id.* at 24-25. For this reason, antitrust scholars

applaud the elimination of this phenomenon of "double marginalization." *See, e.g.*, 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 758b at 30 (2d ed. 2002).

Second, foreshadowing the Supreme Court's concerns in *Trinko*, Judge Breyer highlighted the adverse administrative considerations that counsel against recognizing price-squeeze claims. These administrative considerations implicate *Alcoa*'s core elements: a "fair price" for the wholesale product and a "living profit" for second-level competitors. Questioning the practicality of administering remedies for an unlawful price squeeze, Judge Breyer asked rhetorically how a judge or jury could determine a fair price or a proper price gap between the wholesale and retail prices. *Town of Concord*, 915 F.2d at 25. What *Trinko* recognized as a fatal flaw in a refusal-to-deal theory—namely, that "[e]nforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited," *Trinko*, 540 U.S. at 408—is, as *Town of Concord* indicates, just as fatal for an *Alcoa* price-squeeze claim. As explained by the current chief economist of the Antitrust Division of the Department of Justice, to determine a "fair price" or a "living profit" for firms that meet some threshold level of efficiency, courts must "become a type of regulatory body setting complex terms . . . in an area where, unlike a regulatory body, the courts have no special expertise." Dennis W. Carlton, *A General Analysis of Exclusionary Conduct and Refusal to Deal—Why* Aspen Skiing *and* Kodak *Are Misguided*, 68 ANTITRUST L.J. 659, 662 (2001).

In sum, it is imperative that the Court grant certiorari in *linkLine* to clarify that the price-squeeze theory is a regulatory undertaking, not an antitrust cause of action. It is neither feasible nor advisable to use antitrust law to make a vertically integrated firm responsible for ensuring the profitability of its competitors in the downstream market. Such a rule would create a powerful incentive for the vertically integrated firm to raise its retail price to reduce the risk of antitrust lawsuits by unprofitable downstream competitors. That result is antithetical to the consumer-welfare objective that animates American antitrust law.

CONCLUSION

For the reasons presented above, the petition for a writ of certiorari should be granted.

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AMICUS CURIAE BRIEF

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IN THE

Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY,
D/B/A AT&T CALIFORNIA, ET AL., PETITIONERS

v.

LINKLINE COMMUNICATIONS INC., ET AL.,
RESPONDENTS

On Petition for a Writ of Certiorari To the United States Court of Appeals For the Ninth Circuit

BRIEF OF VERIZON COMMUNICATIONS INC. AND THE NATIONAL ASSOCIATION OF MANUFACTURERS AS *AMICI CURIAE* SUPPORTING PETITIONERS

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BRIEF OF VERIZON COMMUNICATIONS INC. AND THE NATIONAL ASSOCIATION OF MANUFACTURERS AS *AMICI CURIAE* SUPPORTING PETITIONERS

INTEREST OF *AMICI CURIAE*[1]

Verizon Communications Inc. (Verizon) is one of the largest providers of telecommunications services in the United States. Verizon affiliates provide a variety of wireless and wireline communications services directly to retail customers and, on a wholesale basis, to other communications service providers that compete with Verizon at the retail level. In particular Verizon is competing at both retail and wholesale for broadband services that provide high speed connections to the Internet.

It is widely recognized that the truly important advances in the telecommunications world in the last 10 years are the advances in broadband, not the sharing of old infrastructure. The advances in broadband have taken place in a vigorously competitive world – cable technology versus, first,

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[1] Under S. Ct. R. 37, *amici curiae* states the following: (1) Counsel of record for all parties received notice at least 10 days prior to the due date of the *amici curiae's* intention to file this brief. (2) All parties have consented to the filing of this brief. (3) No counsel for a party has written this brief in whole or in part, and no person or entity other than the amici curiae or their counsel has made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae*, their members, or their counsel made a monetary contribution to their preparation or submission.

DSL technology and, now, fiber optic and wireless technology.[2]

The antitrust litigation by non-facilities-investing firms seeking to piggyback on the old infrastructure starting in the late 1990s was a drain on Verizon and others seeking to focus on broadband progress. The Court in *Trinko* rightly brought that litigation to an end, recognizing that the litigation powerfully undermined, rather than served, the goals of antitrust law. Now the Ninth Circuit, in conflict with four other circuits, has resurrected a means to create all the harm that this Court had stopped in *Trinko*.

With respect to high-speed services like the one at issue here, following the Court's decision in *Trinko* and the FCC's parallel decision under the 1996 Telecommunications Act to stop requiring telephone companies to share their broadband networks, Verizon has been investing vast sums to deploy a fiber optic network to consumers.[3] Verizon has a

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[2] *See, e.g.*, FCC, Wireline Competition Bureau, Indus. Analysis & Tech. Div., *High-Speed Services for Internet Access* (Oct. 2007), available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-277784A1.pdf; *Time Warner Telecom, Inc. v. FCC*, 2007 U.S. App. LEXIS 24204 (3d Cir. Oct. 16, 2007) (dismissing challenges to the FCC's removal of common carrier regulations from telephone company broadband services).

[3] Verizon is investing $23 billion to offer fiber optic connections to 18 million households by 2010. *See* Leslie Cauley, *Verizon's army toils at daunting upgrade*, USA Today, Oct. 25, 2007; Verizon press release (Oct. 29, 2007), available at http://investor.verizon.com/news/view.aspx?NewsID=863 (Verizon's fiber-to-the-premises network currently passes 8.5 million premises). Verizon is the first major telecom company to deploy gigabit passive optical network (G-PON) technology to customers in the

strong interest in the development of sound antitrust principles that neither cap prices on services deriving from beneficial (and risky) investments nor penalize retail price reductions that benefit consumers by intensifying competition against rivals (like cable). Verizon urges this Court to review the decision below and to reject categorically a Sherman Act § 2 "price squeeze" claim as inconsistent with precedent and important antitrust policies, including those requiring clear guidelines for unilateral business conduct.

The National Association of Manufacturers is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. The NAM's mission is to enhance the competitiveness of manufacturers by shaping a legislative and regulatory environment conducive to U.S. economic growth and to increase understanding among policymakers, the media and the general public about the vital role of manufacturing to America's economic future and living standards.

SUMMARY OF ARGUMENT

I. The Ninth Circuit's ruling is at odds with this Court's decisions in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), and *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004). *Brooke Group* held that above-cost retail prices do not constitute predatory pricing under Section 2, and *Trinko* held

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United States which dramatically increases internet access speeds. Verizon press release (Mar. 27, 2007), available at http://investor.verizon.com/news/view.aspx?NewsID=825.

that a firm in the position of petitioner here does not violate Section 2 by refusing to sell goods at wholesale to a rival. Together, those decisions prove that a dominant firm in petitioner's position does not violate Section 2 by failing to sell a rival goods at a wholesale price that enables that competitor to make a profit at the retail level. Four other circuit courts – the D.C., Fourth, Seventh, and Eleventh Circuits – have expressly so held.

II. Even more broadly, recognizing price squeeze liability claims under Section 2 would disrupt the policies underlying that law. All firms should be free both to integrate vertically and to price competitively unless those practices threaten to drive rivals from the market and harm competition. This Court addressed that precise concern in *Brooke Group* and ruled that a price discount is not predatory unless it both is below cost and poses a dangerous risk of subsequent monopoly pricing. The same rule should be applied here. A so-called price squeeze typically reflects the decision of a vertically-integrated firm voluntarily to offer a good to a competitor at wholesale and to compete vigorously over price at retail. Both practices are beneficial and should be encouraged.

The Ninth Circuit's rule, by contrast, will deter such sales and pricing competition. Firms will limit investments or restrict output due to fear of liability for charging too much at the wholesale level or too little at the retail level; they will avoid selling at wholesale to rivals due to fear of liability for charging too much; they will raise their retail prices or forgo price reductions due to fear of liability for charging

too little; or they will do all of the above. There is no good reason to incur those harms.

III. The Ninth Circuit's rule creates uncertainty in an area – pricing – where this Court has sought to bring certainty and stability to antitrust law. This Court in *Brooke Group* adopted an objective test to determine when price is used as a predatory weapon to ensure that the bench, bar, and business community could apply the law in a predictable manner. The Ninth Circuit's decision, by contrast, forces juries, antitrust counselors, and managers to decide what wholesale and retail prices leave a rival with the opportunity to secure a "reasonable" profit. Yet, for more than a century it has been settled law that no trier of fact should be tasked with the burden of calculating a "reasonable" price in an antitrust case. By ignoring that settled proposition, the Ninth Circuit in this case has repeated the same mistake that it made in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069 (2007), of directing the common law judicial system to answer a question fit (at best) only for regulators.

ARGUMENT

THE ALLEGATION THAT A VERTICALLY-INTEGRATED MONOPOLIST'S WHOLESALE AND RETAIL PRICES CREATE AN UNLAWFUL "PRICE SQUEEZE," AT LEAST WHERE THE MONOPOLIST HAS NO ANTITRUST DUTY TO DEAL, FAILS TO STATE A CLAIM UNDER SHERMAN ACT § 2

I. THE NINTH'S CIRCUIT'S RULING CONFLICTS WITH OTHER CIRCUIT COURT DECISIONS

As Chief Judge (and former Assistant Attorney General for the Antitrust Division) Douglas Ginsburg explained for the D.C. Circuit, there is no merit to the allegation that a vertically-integrated monopolist that lacks an antitrust duty to deal has created an unlawful "price squeeze" by setting its wholesale and retail prices in such a manner that a rival cannot make a profit. *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673 (2005). The unanimous panel rejected the price squeeze claim, involving the same type of dual wholesale and retail sales of broadband services as here, as a matter of law. Relying on this Court's 2004 decision in *Trinko*, which held that Sherman Act § 2 does not impose on a dominant firm a duty to deal with a rival, the court of appeals held that, if a monopoly has no duty to deal with a rival in the first place, it has no obligation to ensure that its rival makes a profit when it volunteers to do business with that rival nonetheless. Chief Judge Ginsburg's decision endorsed the analysis of one of the nation's leading antitrust scholars, Professor Herbert Hovenkamp: "it makes no sense to prohibit a predatory price squeeze in

circumstances where the integrated monopolist is free to refuse to deal." 398 F.3d at 673, quoting 3A Philip E. Areeda & Herbert Hovenkamp, *Antitrust Law* 129-30 (2d ed. 2002).

The Ninth Circuit in this case agreed, as it had to under this Court's decision in *Trinko*, that petitioners do *not* have a duty to sell the products here at wholesale to respondents. A divided Ninth Circuit panel nevertheless permitted respondents to assert a price-squeeze claim based on the relative wholesale and retail prices. The panel majority held that "a price squeeze occurs when a vertically integrated company sets its prices or rates at the first (or upstream) level so high that its customers cannot compete with it in the second-level (or downstream) market." Slip op. at 12187 (citation and quotation marks omitted).

The Ninth Circuit stands alone in reaching this decision. In addition to the D.C. Circuit, the Fourth and Seventh Circuits rejected, at the motion to dismiss stage, price squeeze claims indistinguishable from the one that the Ninth Circuit endorsed in this case.[4] Similarly, the Eleventh Circuit limited "price

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[4] The Fourth Circuit upheld dismissal on the pleadings of a complaint that "Verizon's provision of its last-mile facilities" at wholesale to rival Cavalier was "overly ... expensive" and that Verizon offered its own retail services "at a price lower than Cavalier's 'retail' cost ..., or at a price so low that Cavalier could not profitably offer such services" in competition with Verizon. *Cavalier Telephone v. Verizon Virginia*, 330 F.3d 176, 180-81 (4th Cir. 2003), *cert. denied*, 540 U.S. 1148 (2004). The Seventh Circuit, in an opinion written by Judge Diane Wood (who was former Deputy Assistant Attorney General for Antitrust), upheld dismissal on the pleadings of a complaint that "Ameritech has refused to sell to its competitors local telephone

squeezing" antitrust theories to the predatory pricing framework established by this Court in *Brooke Group*: a pricing complaint "must contain ... the two basic prerequisites for a showing of price predation" – prices must be "below an appropriate measure of ... costs" and there must be "a dangerous probability[] of recoup[ment]."[5]

The First Circuit, in an opinion by then-Judge Breyer, expressed strong skepticism about price squeeze liability in an unregulated industry.[6] The court wrote that it must "take account of the institutional fact that antitrust rules are court-

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services at wholesale prices that are just, reasonable, and nondiscriminatory, which prevents the competitors in turn from offering attractive resale prices to consumers." *Goldwasser v. Ameritech Corp.*, 222 F.3d 390, 395 (7th Cir. 2000).

[5] *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050 (11th Cir. 2004), *cert. denied*, 544 U.S. 904 (2005), quoting *Brooke Group*, 509 U.S. at 222. The plaintiff in that case filed a rehearing petition noting correctly that the Eleventh Circuit's "Opinion ... treats Covad's 'price squeeze' claim as if it were a 'predatory pricing' claim and applies the standards of *Brooke Group* ...." Appellants' Petition for Rehearing at 1, *Covad Communications Co. v. BellSouth Corp.*, No. 01-16064-C (11th Cir. filed July 16, 2004). The Eleventh Circuit denied rehearing. The D.C. Circuit similarly read the Eleventh Circuit's decision as requiring pricing complaints, where there is no duty to deal at wholesale, to meet the strict standards for predatory pricing. *Covad Communications Co. v. Bell Atlantic Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005) (discussing sister case against BellSouth).

[6] *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990). The First Circuit's holding extended only to a rejection of price squeeze liability for firms whose prices are regulated at both wholesale and retail levels, but the skepticism noted in text was stated in the context of fully *un*regulated firms. *See id.* at 23.

administered rules"[7] but even in a fully unregulated context "it is not easy for courts to administer Judge Hand's [*Alcoa*] price squeeze test"[8]:

> That test makes it unlawful for a monopolist to charge more than a "fair price" for the primary product while simultaneously charging so little for the secondary product that its second-level competitors cannot make a "living profit." *See Alcoa*, 148 F.2d at 437-38. But how is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will?

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[7] 915 F.2d at 22.

[8] 915 F.2d at 25, discussing *United States v. Aluminum Co.*, 148 F.2d 416 (2d Cir. 1945).

> We do not say that these questions are unanswerable, but we have said enough to show why antitrust courts normally avoid direct price administration ***.[9]

Outside the Ninth Circuit, at least where there is no duty to deal (as rarely exists and, the Ninth Circuit agreed, does not exist in this case), the Sherman Act does not forbid a vertically-integrated firm – even one possessing monopoly power – from setting above-cost profit-maximizing prices at both levels. This clear conflict among the circuits requires resolution by this Court.

II. THE NINTH CIRCUIT'S RULING IS INCONSISTENT WITH THIS COURT'S PRECEDENTS AND SETTLED ANTITRUST PRINCIPLES

This Court's decisions, most importantly *Trinko*, *Brooke Group*, and *Weyerhaeuser*, recognize that Section 2 must not condemn single-firm conduct as anticompetitive if doing so will deter activity that typically is legitimate and, indeed, to be encouraged. That fundamental approach requires rejection of the Ninth Circuit's "price squeeze" basis for potential Section 2 liability. For price competition in particular, the principles recognized in *Trinko*, *Brooke Group*, and *Weyerhaeuser* all compel the conclusion that any concern in this area should be left to the predatory pricing standards already established in the law, and not expanded to embrace non-predatory "price squeezes." This Section focuses

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[9] 915 F.2d at 25. Yet another circuit judge, J. Posner, has written more bluntly, "now that the *Alcoa* doctrine is defunct, it is understood that a monopolist is free to compete ...." R. Posner, *Antitrust Law* 250 (2d ed. 2001).

on the substantive antitrust reasons for that conclusion, which are then powerfully reinforced, as explained in Point III, by the concerns about the institutional capacity of juries in antitrust cases to make the judgments inherent in any "price squeeze" claim.

A. The Ninth Circuit's price squeeze theory necessarily questions whether the wholesale prices are too high. But *Trinko* establishes not only that Section 2 supplies no basis for such a concern, but that grave antitrust *harm* can easily result from allowing challenges whose mere threat unavoidably would limit prices of a legitimate monopolist. The combination of reasons that led to rejection of a duty to deal there should not be undermined by a price squeeze alternative way of doing what *Trinko* stopped. Indeed, the very complaint in *Trinko* was substantively equivalent to a "price squeeze" – the retail competitors there allegedly couldn't survive against the wholesaler's retail prices given what they had to pay for the wholesale product and the quality of what they got.

Antitrust positively values the freedom to charge prices without caps if the monopoly is lawful. "The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system" because it "attracts 'business acumen'" and "induces risk taking that produces innovation and economic growth." 540 U.S. at 407.[10]

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[10] The Justice Department agrees "a firm should not be required to sacrifice profits to sell to competitors at a discount, even if that would on balance produce social gains; therefore, a monopolist's refusal to sell below the monopoly price should not

In addition, the fundamental limits on the institutional capacity of courts and juries, which must limit what Section 2 covers, are particularly strained in pricing cases. As described above, this point was central to Judge Breyer's opinion in *Town of Concord* rejecting price squeeze liability for regulated firms. The Ninth Circuit's decision creates a more difficult regime than the Second Circuit created in *Trinko*. Here, courts and juries must evaluate not one but two sets of prices and terms.

B. The dangers of a price squeeze theory's inhibition on wholesale prices as too high are at least matched by the dangers of such a theory's challenges to retail prices as too low. *Brooke Group*, reinforced by *Weyerhaeuser*, recognizes those dangers and insists on stringent conditions focused on the defendant's own cost-price characteristics before any Section 2 liability can be imposed. Those conditions should govern in this setting, too.

Brooke Group recognized that a company's above-cost price reductions can threaten the profitability of less efficient rivals, but discounts benefit consumers

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be a violation, because that would require that the monopolist share its profits." J. Bruce McDonald, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Remarks to the College of Europe, Global Competition Law Centre, The Modernization of Article 82 Second Annual Conference: Section 2 and Article 82: Cowboys and Gentlemen (June 16-17, 2005). *See* Herbert Hovenkamp, *The Legal Periphery of Dominant Firm Conduct*, University of Iowa Legal Studies Research Paper, No. 07-21, at 5 (Sept. 2007), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1014426 ("United States [law provides] unambiguously that once the monopolist has attained its position it may charge any price that the market will bear.").

nonetheless, at least in the short run, regardless of how prices are set.[11] *Brooke Group* also acknowledged that weaknesses in the legal system render it inherently incapable of effectively identifying and deterring only a limited category of disfavored above-cost discounts. Any rule outlawing some disfavored above-cost discounts would end up deterring a larger number of social welfare-enhancing above-cost discounts by risk-averse firms. Accordingly, the Court adopted a stringent test for predation: A plaintiff must prove both that the defendant has engaged in short-run below-cost pricing and reasonably could expect to recoup those losses via long-run monopoly pricing. That test was necessary in order to avoid chilling aggressive price competition. Because the benefits to consumers of discounts are immediate and desirable and the occasions for their proper condemnation rare, this Court approved a limited, simple, and objective standard that readily can be understood and applied by courts, juries, practitioners, and businesses. 509 U.S. at 223-26.

C. This Court revisited the issue of predation last Term in *Weyerhaeuser* and applied the *Brooke Group*

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[11] *See* Thomas O. Barnett, Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Opening Remarks at the Antitrust Division and FTC Hearings Regarding Section 2 of the Sherman Act: The Gales of Creative Destruction: The Need for Clear and Objective Standards for Enforcing Section 2 of the Sherman Act (June 20, 2006) ("In *Brooke Group*, the Court recognized the possibility that above-cost pricing might hurt competition but nonetheless insulated above-cost pricing from liability to avoid the greater harm of a legal regime that would cause firms to hesitate before lowering their prices or not to lower prices at all.").

test to a claim that above-cost *purchases* were anticompetitive. The Court reiterated that pricing conduct playing a commonplace role in legitimate market competition must not be chilled by uncertain liability standards. 127 S. Ct. at 1074-75. "We were particularly wary [in *Brooke Group*] of allowing recovery for above-cost price cutting because allowing such claims could, perversely, 'chill legitimate price cutting,' which directly benefits consumers." *Id.* at 1074.[12] The Court then compared the economics and real-world practices of predatory pricing and predatory bidding, finding that, since the economics underlying the two practices is "analytically similar" and the claims of injury were "strikingly similar," the same antitrust rule should apply in both settings. *Id.* at 1076-77.

The reasoning in *Weyerhaeuser* is particular relevant here. The defendant there was a market intermediary; it purchased inputs from upstream suppliers and combined them with other inputs to create products sold downstream. The Court held that a plaintiff who sues an intermediary for "predatory bidding" must prove, among other things that the defendant's supposedly inflated purchase prices "caused the cost of the relevant output to rise above the revenues generated in the sale of those outputs." 127 S. Ct. at 1078. The "relevant output" in that context — a retail product — is analogous to

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[12] *See also id.* at 1075 (cost of erroneous findings of predatory-pricing liability is "quite high" because "the mechanism by which a firm engages in predatory pricing – lowering prices – is the same mechanism by which a firm stimulates competition;" "mistaken findings of liability would chill the very conduct the antitrust laws are designed to protect") (citations omitted).

the retail service involved here. And the Court's holding requires a comparison of the aggregate cost of all inputs to the price charged for a defendant's retail product. The sustainability of the particular *plaintiff's* business is of no moment if the stringent standard, based entirely on the defendant's costs and prices, is not met.

Here, by analogy, when a plaintiff sues a defendant for a supposed price squeeze, the relevant cost-price comparison should focus on the *defendant's* profit-making ability, *not* the *plaintiff's*. As in *Brooke Group* and *Weyerhaeuser*, keeping the focus entirely on the integrated firm's costs and prices reflects any advantages or disadvantages that the integrated firm may have, such as scope economies or burdens of legacy processes or equipment, avoids penalizing low retail pricing that benefits retail customers, and prevents antitrust doctrine from being used to shelter inefficient practices by competitors. The only proper comparison should remain between the total cost of all inputs in the defendant's retail service and the defendant's retail price of that service, not *the plaintiff's* prices and costs. Yet the latter is the essence of the Ninth Circuit's "price squeeze" doctrine.

The path taken in *Brooke Group* and *Weyerhaeuser* should be followed here. A so-called price squeeze typically reflects the decision of a dominant vertically-integrated firm voluntarily to offer a good to a competitor at wholesale while vigorously competing against that rival over price at retail. The two practices benefit consumers through increased competition and lower prices and therefore should be encouraged. In fact, if the retail competitor is more

efficient and thus has lower costs than the integrated firm, it generally is in the integrated firm's best interest to sell to the competitor, not to exclude it.[13] It might even be desirable for the integrated firm to exit the retail level and rely entirely on the more efficient competitor for distribution of its product or service. In addition, if there is competition in the sale of the upstream product, *i.e.*, the upstream producer is *not* a monopolist, then a price squeeze could only occur by the integrated producer lowering its downstream price, inasmuch as it could not raise its upstream price in a competitive market. In this circumstance, the antitrust analysis is identical to that of predatory pricing and there is no need of a separate "price squeeze" theory of antitrust liability.

The upshot is this: The only setting in which the combination of practices at issue here is likely to raise material concerns about competitive harm is the setting already identified in *Brooke Group* and *Weyerhaeuser* – where a firm sells at a loss downstream in order to drive a rival from the market, and then recoups the loss by charging higher prices. But the *Brooke Group-Weyerhaeuser* test already defines when such conduct can be condemned as

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[13] "An unusual feature of a margin squeeze is that the downstream rival is at the same time a customer of the dominant firm upstream. Thus, by excluding a downstream rival, the dominant firm also reduces its upstream profits because it would also lose a customer. This dynamic can have substantial effects on the incentives for such conduct and may in fact amount to a disincentive to engage in a margin squeeze in the first place." Damien Geradin & Robert O'Donoghue, *The Concurrent Application of Competition Law and Regulation: the Case of Margin Squeeze Abuses in the Telecommunications Sector* 11 (Apr. 2005).

anticompetitive. The price squeeze doctrine approved by the Ninth Circuit, therefore, is overbroad and affirmatively harmful to social welfare.

D. The ruling below will have several adverse effects on the competitive process. When there is no duty to deal, the threat of a price squeeze challenge creates incentives not to deal, even though there would be benefits to rivals and consumers from dealing. The resulting harm to consumers can be especially great when a downstream firm uses a dominant firm's input to produce a third downstream product that the monopolist does not itself produce. Choosing not to deal thus would deny consumers the benefits derived from the third product. When there is a duty to deal, inefficiencies are created as a firm raises its retail price or withdraws from the retail market in an effort to reduce its liability. Accordingly, the Ninth Circuit's ruling will injure the very parties that it sought to protect.

The Ninth Circuit's decision will cause systemic injuries to the competitive process, too. To start with, the decision below could disrupt the beneficial innovation and investment by facilities-based competitors under the FCC's 2005 decision to free telephone companies from the prior duty to grant rival Internet service providers wholesale access to their facilities.[14] Some firms will be deterred from internal growth; they may limit risky investments that depend on freedom to charge market-bearing

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[14] *In re Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, 20 F.C.C.R. 14,853 (2005), *aff'd, Time Warner Telecom, Inc. v. FCC*, Nos. 05-4769 *et al.*, 2007 U.S. App. LEXIS 24204 (3d Cir. Oct. 16, 2007).

upstream prices; they may forgo downstream price cuts; or they may pursue all of the above. Consumers lose when a company that is relatively more efficient than its rivals engages in less aggressive competition for fear of treble damages liability.

III. THE NINTH CIRCUIT'S RULE CREATES UNCERTAINTY WHERE CLARITY IS NEEDED

The Ninth Circuit's decision fails to recognize the need for legal rules that are clear, understandable, and manageable by the bench, bar, and business community. Last Term, this Court granted certiorari in *Weyerhaeuser* to review a Ninth Circuit decision that created a similar problem. Rather than use the *Brooke Group* test to evaluate a "predatory buying" claim, the Ninth Circuit permitted a jury to decide whether such a claim had merit by asking whether the defendant had purchased more raw materials "than it *needed*" from upstream suppliers or had paid a higher price for those materials "than *necessary*, in order to prevent [rivals] from obtaining the [materials] they needed at a *fair* price."[15] Although this Court decided the *Weyerhaeuser* case on a different ground, the issue whether such jury instructions permitted a trier of fact rationally to interpret and apply the Sherman Act was before this Court.

Here, the Ninth Circuit has committed the same type of error: namely, construing Sherman Act § 2 in a manner that leaves it to the jury to decide whether

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[15] *Confederated Tribes of Siletz Indians v. Weyerhaeuser*, 411 F.3d 1030, 1039 n.30 (9th Cir. 2005) (reprinting jury instructions; emphasis added); *see* 127 S. Ct. at 1073.

the defendant has selected "reasonable" prices at two levels. The inevitable consequence of allowing respondents' price squeeze claim to go forward is that at some point the trier of fact may have to decide what is the "reasonable" profit that respondents were denied. Yet, this Court has repeatedly noted that there is no question our common law system is *less* fit to decide than whether a particular price is "reasonable," either in the abstract or as applied.[16] Judges have no special expertise to second-guess the market as to what price is "reasonable."[17] Allowing

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[16] *See, e.g., United States v. Trenton Potteries Co.*, 273 U.S. 392, 397-98 (1927) (rejecting claim that the Sherman Act outlaws only the fixing of an "unreasonable" price due to difficulty of making that finding); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 283 (6th Cir. 1898) (Taft, J.) (to examine reasonableness of price is to "set sail on a sea of doubt"), *aff'd*, 175 U.S. 211 (1899); *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, J.), quoted in text at page 9; David S. Evans & A. Jorge Padilla, *Excessive Prices: Using Economics to Define Administrable Legal Rules*, 1 J. of Competition Law & Econ. 97, 100 (2005) ("There is no generally accepted definition of what an 'unfair' price is."); Herbert Hovenkamp, *Post-Chicago Antitrust: A Review and Critique*, 2001 Colum. Bus. L. Rev. 257, 293 ("Coming up with the right price is a completely intractable problem for several reasons."); Paul L. Joskow, *Transaction Costs Economics, Antitrust Rules, and Remedies*, 18 J. Law, Econ. & Org. 95, 100 (2002); Donald F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 Harv. L. Rev. 655, 670 (1962); *cf. City of Milwaukee v. Illinois*, 451 U.S. 304, 325 (1981).

[17] "Markets are much better than judges at sifting efficient from anticompetitive practices." Frank H. Easterbrook, *Contract and Copyright*, 42 Hous. L. Rev. 953, 957 (2005). *See* Thomas O. Barnett, Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Presented at the Fordham Competition Law Institute,

juries to make that call would produce radically indeterminate results from one case to the next, because no two juries (or jurors) will share the same intuitions about what above-cost prices are "reasonable."[18]

Price-setting is a job almost always done best by the market, only rarely done adequately by regulators, and never done satisfactorily by courts. This Court made that point in *Trinko*, noting that courts should impose no antitrust duty that "'requires the court to assume day-to-day controls characteristic of a regulatory agency.'"[19] If the law is to replace the

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34th Annual Conference on International Antitrust Law & Policy: Section 2 Remedies: A Necessary Challenge (Sept. 28, 2007) (prescribing the "advice of Hippocrates" for Section 2 – "at least ... do no harm," noting: "markets change in ways we cannot predict"; "imposing a duty on a defendant to provide competitors access to its assets ... can undermine the incentive of those other competitors to develop their own assets as well as undermine the incentive for the defendant competitor to develop the assets in the first instance"); J. Bruce McDonald, The Modernization of Article 82 Second Annual Conference: Section 2 and Article 82: Cowboys and Gentlemen ("Forced sharing also requires courts to determine when resources are competitively advantageous and indispensable and at what price they should be made available, a set of decisions better left to the market.").

[18] "When the judge himself lacks the skills to determine whether an expert's report is technically accurate, the worst possible outcome is the one that too often obtains: the judge washes his hands of the matter and gives it to the jury, thus passing the issue off to an even less qualified decision maker." Herbert Hovenkamp, *The Rationalization of Antitrust Law*, 116 Harv. L. Rev. 917, 942-43 (2003).

[19] *Trinko*, 540 U.S. at 415 (quoting Philip E. Areeda, *Essential Facilities: A Doctrine in Search of Limiting Principles*, 58 Antitrust L.J. 841, 853 (1989)). *See* Antitrust Modernization Commission, Report and Recommendations 105 (Apr. 2007)

market at setting a price, firms need a clear, ex ante pricing rule so that they can decide what decisions to make. A legal rule that rests on a lay jury's after-the-fact estimation whether a price was "reasonable" is anything but clear.

Contrary to what the majority below assumed, reliance on the Rule of Reason is not helpful when pricing is at issue. That approach would not filter out early in the process, at the point before litigation, when businesses need guidance the most, cases that could not pose the type of harm *Brooke Group* feared. The result would be to force the courts to engage in a broad and essentially standardless inquiry into the particular facts and circumstances of each plaintiff company's demand for a "reasonable" profit.

("Moreover, forced sharing requires courts to determine the price at which such sharing must take place, thereby transforming antitrust courts into price regulators, a role to which they are ill-suited."). *See also* Thomas O. Barnett, 34th Annual Conference on International Antitrust Law & Policy: Section 2 Remedies: A Necessary Challenge (Sept. 28, 2007) ("The remedy should use market competition to the greatest extent possible to achieve its ends and should minimize the regulatory restraints, such as market share caps, price regulations or other behavioral restrictions....Suffice it to say that agencies and courts lack the resources and expertise to run business in an efficient manner.").

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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JOINT APPENDIX

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IN THE

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PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

JOINT APPENDIX

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NOTICE

The following documents have been omitted in the printing of this Joint Appendix but may be found in the appendix to the petition for a writ of certiorari in this case:

Opinion of the United States Court of Appeals for the Ninth Circuit, *linkLine Communications, Inc., et al. v. SBC California, Inc., et al.*, No. 05-56023 (Sept. 11, 2007) 1a

Order Granting in Part and Denying in Part Defendant's Motion To Strike Portions of Plaintiff's First Amended Complaint, To Dismiss the First Amended Complaint, or To Certify October 20, 2004, Order for Interlocutory Appeal, *link-Line Communications, Inc., et al. v. SBC California, Inc., et al.*, No. CV 03-5265 SVW (SHx) (C.D. Cal. Apr. 1, 2005) 25a

Order Granting in Part and Denying in Part Defendants' Motion for Judgment on the Pleadings, *linkLine Communications, Inc., et al. v. SBC California, Inc., et al.*, No. CV 03-5265 SVW (SHx) (C.D. Cal. Oct. 20, 2004) 58a

Order of the United States Court of Appeals for the Ninth Circuit Granting Petition for Permission To File Interlocutory Appeal, *SBC California, Inc., et al. v. linkLine Communications, Inc., et al.*, No. 05-80033 (July 18, 2005) 92a

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

No. CV 03-5265 SVW (SHx)

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants.

DOCKET PROCEEDINGS

DATE	#	DOCKET ENTRY
7/24/03	1	COMPLAINT filed Summons(es) issued referred to Discovery Stephen J. Hillman (jag) (Entered: 07/28/2003)
		* * * * *
9/15/03	5	ANSWER filed by defendant SBC California Inc to complaint [1-1] (yc) (Entered: 09/16/2003)
		* * * * *
7/6/04	16	NOTICE OF MOTION AND MOTION for Judgment on the Pleadings filed by defendants Pacific Bell Internet Services, SBC Advanced Solutions Inc, SBC California Inc. Motion set for hearing on 9/20/2004 at 01:30 PM before Honorable Stephen V. Wilson. (yc) (Entered: 07/07/2004)

7/6/04	17	REQUEST FOR JUDICIAL NOTICE re MOTION for Judgment on the Pleadings 16 filed by defendants Pacific Bell Internet Services, SBC Advanced Solutions Inc, SBC California Inc. (yc) (Entered: 07/07/2004)
8/6/04	18	OPPOSITION to Defendants' MOTION for Judgment on the Pleadings 16 filed by Plaintiffs Inreach Internet LLC, Nitelog Inc, Om Networks, linkLine Communications Inc. (rl) (Entered: 08/10/2004)
9/3/04	19	REPLY MEMORANDUM in Support of Motion for Judgment on the Pleadings 16 filed by Defendants Pacific Bell Internet Services, SBC Advanced Solutions Inc and SBC California Inc. (yl) (Entered: 09/09/2004)

* * * * *

10/20/04	23	Order by Judge Stephen V. Wilson that Defendants MOTION for Judgment on the Pleadings 16 is GRANTED IN PART and DENIED IN PART. Further, because plaintiffs price-squeeze claim which do not derive from Trinko, the Court ORDERS plaintiffs to file with the Court an amended complaint limited to the price-squeeze claim that details beyond the normal requirements of Rule 8 specific facts supporting Plaintiffs' price-squeeze claim. Finding Request for Judicial Notice, Request for Relief 17 as MOOT. (el) (Entered: 10/25/2004)

10/20/04	24	SUBMISSION OF ADDITIONAL AUTHORITY re MOTION for Judgment on the Pleadings 16 filed by Defendants Pacific Bell Internet Services, SBC Advanced Solutions Inc, SBC California Inc. (el) (Entered: 10/27/2004)

* * * * *

12/7/04	26	FIRST AMENDED COMPLAINT against Defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc amending Complaint – (Discovery) 1, filed by Plaintiffs linkLine Communications Inc, Inreach Internet LLC, Om Networks, Nitelog Inc (el) (Entered: 12/13/2004)
1/14/05	27	NOTICE OF MOTION AND to Strike portions of plaintiffs first amended complaint, to Dismiss the first amended complaint, to Certify October 20, 2004, Order for interlocutory appeal filed by defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc. Motion set for hearing on 2/14/2005 at 01:30 PM before Honorable Stephen V. Wilson. Lodged Order. (ca) (Entered: 01/21/2005)
1/14/05	28	MEMORANDUM in Support of MOTION to Strike portions of plaintiffs first amended complaint, to Dismiss the first amended complaint, or to Certify October 20, 2004, Order for interlocutory appeal 27 filed by

		defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc. (ca) (Entered: 01/21/2005)
1/14/05	29	DECLARATION of Jason Murray in support of MOTION to Strike portions of plaintiffs first amended complaint, to Dismiss the first amended complaint, or to Certify October 20, 2004, order for interlocutory appeal 27 filed by defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc. (ca) (Entered: 01/21/2005)
1/28/05	30	OPPOSITION to MOTION to Strike Portions of and to Dismiss First Amended Complaint, or to Certify 27 filed by Plaintiffs linkLine Communications Inc, Inreach Internet LLC, Om Networks and Nitelog Inc. (yl) (Entered: 02/02/2005)
2/4/05	31	REPLY in support of MOTION to Strike portions of plaintiffs first amended complaint, to Dismiss the first amended complaint, to Certify October 20, 2004, Order for interlocutory appeal 27 filed by Defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc. (shb) (Entered: 02/08/2005)

* * * * *

3/4/05	34	Defendants' SUBMISSION OF ADDITIONAL AUTHORITY filed by Defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc. (shb) (Entered: 03/07/2005)
3/7/05	35	REPLY filed by Plaintiffs linkLine Communications Inc, Inreach Internet LLC, Om Networks, Nitelog Inc re Post Hearing Submission of New Authority 34 (mu) (Entered: 03/14/2005)
3/18/05	36	RESPONSE to Brief filed by Defendants SBC California Inc, Pacific Bell Internet Services, SBC Advanced Solutions Inc re Reply (non-motion) 35 (mu) (Entered: 03/22/2005)
4/1/05	37	ORDER by Judge Stephen V. Wilson Granting in Part and Denying in Part Defendant's Motion to Strike Portions of Plaintiff's First Amended Complaint, or to Dismiss the First Amended Complaint, or to Certify 10/20/2004, Order for Interlocutory Appeal. (yl) (Entered: 04/04/2005)
4/26/05	38	MINUTES by Judge Stephen V. Wilson; Pursuant to stipulation of the parties and order to the Court, filed 4/26/05 this matter was stayed pending decision of Ninth Circuit. Court orders this matter placed on its inactive calendar. All dates are vacated. Parties are ordered to notify the Court when this case should be restored to the active calendar. (Made

JS-6. Case Terminated.) Court Reporter: n/a. (jag) (Entered: 04/27/2005)

4/26/05 39 STIPULATION AND ORDER by Judge Stephen V. Wilson that this action is stayed until the later of the Ninth Circuit Court of Appeals resolution of defendants interlocutory appeal of this Courts 10/20/04 order; or the Ninth Circuit Court of Appeals denial of defendants request for interlocutory appeal of this Courts 10/20/04 order. (jag) (Entered: 04/27/2005)

7/18/05 40 ORDER from 9th CCA filed as to Stipulation and Order, 39, CCA # 05-56023. Order received in this district on 7/20/05. The petition for permission to appeal pursuant 28 USC 1292 is granted. Within 10 days of this order, petitioners shall perfect the appeal pursuant to FRAP 5(d). (05-80033) (fvap) (Entered: 07/21/2005)

* * * * *

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 05-56023

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs-Appellees,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants-Appellants.

Appeal from the United States District Court
for the Central District of California
Steven V. Wilson, District Judge, Presiding
D.C. No. CV-03-05265-SVW

DOCKET PROCEEDINGS

DATE	#	DOCKET ENTRY
7/18/05	2	Filed order (Johnnie B. RAWLINSON, Jay S. BYBEE): The petn for permission to appeal is granted. Within 10 days of this order, petnrs shall perfect the appeal pursuant to FRAP 5d. [05-56023]
7/19/05	1	DOCKETED CAUSE AND ENTERED APPEARANCES OF COUNSEL. CADS SENT (Y/N): y. setting schedule as follows: Fee payment is due 8/2/05; CADS is past due; CADS must be filed no later than 7/26/05; appellant's designation of RT is due; appellee's designation of RT is due 8/8/05; appel-

lant shall order transcript by 8/18/05; court reporter shall file transcript in DC by 9/19/05; certificate of record shall be filed by 9/26/05; appellant's opening brief is due 11/4/05; appellees' brief is due 12/5/05; appellants' reply brief is due 12/19/05. [05-56023]

* * * * *

12/5/05 14 Filed original and 15 copies Aplts opening br of 32 pages; 5 Excs. (Informal: n); served on 12/5/05; minor defcy: (needs Statement of Related Cases). Notified counsel. [05-56023]

* * * * *

12/13/05 19 Filed original and 15 copies Verizon Communications, Inc.'s amicus curiae brief of 28 pages in support of aplt's reversal [parties' consent on page 1 footnote 1]; served on 12/12/05 [05-56023]

* * * * *

1/18/06 21 Filed original and 15 copies Aples's ans br of 33 pages; served on 1/18/06 [05-56023]

* * * * *

2/21/06 25 Filed original and 15 copies SBC CALIFORNIA, INC., Pacific Bell Inter, SBC Advanced reply brief (Informal: n) 7 [18~26 pages; served on 2/21/06 [05-56023]

* * * * *

6/5/07	32	ARGUED AND SUBMITTED TO Sidney R. THOMAS, Kim M. WARDLAW, Ronald M. GOULD [05-56023]
9/11/07	36	FILED OPINION: AFFIRMED (Terminated on the Merits after Oral Hearing; Affirmed; Written, Signed, Published. Sidney R. THOMAS, author; Kim M. WARDLAW; Ronald M. GOULD, dissenting.) FILED AND ENTERED JUDGMENT. [05-56023]
10/1/07	38	Filed Aplts' unopposed motion to stay the mandate; served on 10/1/07 (PANEL) [6306696] [05-56023]
10/4/07	39	Filed order (Sidney R. THOMAS) Aplts' unopposed mtn to stay the mandate is granted in part. The mandate is stayed for 21 days to allow the Aplts time to file a petition for a writ of certiorari in the USSC. (phoned/faxed) [05-56023]
10/22/07	41	Received notice from Supreme Court: petition for certiorari filed Supreme Court No. 07-512 filed on 10/17/07. (PANEL) [05-56023]
10/23/07	42	Received Aplts' notice of filing of petition for certiorari (Casefile) [05-56023]

* * * * *

[Attorney Name/Address
Block Omitted]

UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
WESTERN DIVISION

No. CV 03-5265 SVW (SHx)

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants.

COMPLAINT FOR DAMAGES AND INJUNCTIVE RELIEF FOR VIOLATIONS OF ANTITRUST LAWS AND STATE LAW CLAIMS (DEMAND FOR JURY TRIAL)

[Filed July 24, 2003]

The above-named plaintiffs herein file this Complaint for damages and injunctive relief, and, demanding trial by jury, complain and allege as follows:

I.

JURISDICTION AND VENUE

1. This Complaint is filed and these proceedings are instituted against the above-named defendants under Sections 4 and 16 of the Clayton Act (15 U.S.C. §§ 15, 26, respectively) to recover treble damages from and secure injunctive relief against the above-

named defendants for their violations of federal antitrust laws. This Court has original jurisdiction over this federal antitrust claim pursuant to 28 U.S.C. § 1337.

2. Both plaintiffs and defendants transact business, maintain offices and may be found within the Central District of California. The interstate trade and commerce involved and affected by the alleged violations of the antitrust laws was carried on, in part, within this District and some of the unlawful acts described herein were conceived, performed or made effective within this District.

II.

THE PARTIES

3. Plaintiff linkLINE COMMUNICATIONS, INC. ("linkLine") is a corporation organized and existing under the laws of the State of Delaware with its principal place of business in Ontario, California. linkLine is an Internet service provider ("ISP") which provides access to the Internet and related services.

4. Plaintiff InReach Internet LLC ("InReach") is a corporation organized and existing under the laws of the State of California with its principal place of business in Stockton, California. InReach is an ISP which provides access to the Internet and related services.

5. Plaintiff Om NETWORKS, d/b/a OMSOFT TECHNOLOGIES, INC. ("Omsoft") is a corporation organized and existing under the laws of the State of California with its principal place of business in Davis, California. Omsoft is an ISP which provides access to the Internet and related services.

6. Plaintiff NITELOG, INC., d/b/a RED SHIFT INTERNET SERVICES ("Red Shift") is a corporation

organized and existing under the laws of the State of California with its principal place of business in Monterey, California. Red Shift is an ISP which provides access to the Internet and related services.

7. Defendant SBC California, Inc. ("SBC") (formerly known as Pacific Bell Telephone Company or "PacBell") is a corporation organized and existing under the laws of the State of California with its principal place of business in San Ramon, California. SBC has authority to operate as a Local Exchange Carrier ("LEC"), providing local telephone services to California consumers within PacBell's local service area. SBC is a subsidiary of SBC Communications, Inc. On September 17, 1998, SBC received approval from the California Public Utilities Commission ("CPUC"), in Resolution T-16191, to provide Digital Subscriber Line ("DSL") services to California consumers.

8. Defendant Pacific Bell Internet Services ("PBI") is a corporation organized and existing under the laws of the State of California with its principal place of business in San Ramon, California. PBI is a subsidiary of SBC. Consumers who ordered SBC's DSL and chose PBI as their ISP were billed the associated fee for Internet access on their regular monthly Pacific Bell telephone billing statement under the heading "Pacific Bell Internet Services."

9. Defendant SBC Advanced Solutions, Inc. ("SBC-ASI") is a Delaware organized [*sic*] and existing under the laws of the State of Delaware corporation [*sic*], with its principal place of business in Houston, Texas. SBC-ASI is a subsidiary of SBC Communications, Inc., and an affiliate of SBC. In June 2000, responsibility for provisioning and billing of DSL was transitioned from SBC to SBC-ASI and the CPUC granted SBC-ASI a certificate of public

convenience and necessity to operate as a facilities-based provider of competitive local exchange and intraLATA interexchange services. SBC-ASI has since and now provides DSL and other advanced services to independent ISP and California consumers.

10. Defendants SBC, PBI, and SBC-ASI are sometimes collectively referred to as the "SBC entities" or "defendants."

III.

NATURE OF TRADE AND COMMERCE AND RELEVANT MARKETS

11. One of the relevant markets in this case is the market for Digital Subscriber Lines in [*sic*] ("DSL") SBC's telecommunication service region in California, which encompasses the vast majority of the State of California's residential and business users. DSL is distinguished from other means of connecting to the Internet because it is (a) faster, (b) "always on," (c) more reliable, and (d) allows many users in the same geographic area simultaneous access without affecting the speed or quality of the transmission. DSL is also distinguishable in that it can be made available over existing telephone lines which today connect virtually all businesses and households in California. There is a discrete and separate market for DSL because of its distinct characteristics, pricing points and separate and distinct customer demand.

12. Another relevant market in this case is the market for Internet services in SBC's California service region. Users of the Internet demand and rely upon ISPs to provide them with access to the Internet and emails for the creation of home page web sites, advertising, means of selling and collecting from purchasers and other related services which

make the Internet commercially useful. Another relevant market is switched local exchange telecommunications service in SBC's California service region. SBC, the incumbent local exchange carrier, has held and holds monopoly power in that local service market, which it has used to dominate DSL and Internet service markets in California, by its monopoly control and manipulation of essential "bottleneck" local telephone network facilities (including the "last mile" connection to end users premises) through which local telecommunication services are provided, including DSL-Internet services, and which cannot practically or reasonably be duplicated.

13. The Internet allows users to access an almost unlimited amount of information in a manner and speed that was previously unavailable. Moreover, the Internet allows groups and individuals to discover and then interact with one another on the basis of common interest. The Internet has transformed the way research is conducted, the way commerce is transacted and the means of buying and selling. In order for all segments of society to make full use of the Internet resources, there must be affordable access to the Internet.

14. Telecommunications companies as a group provide the backbone and distribution plant for Internet transmission and the gateway by which users access the Internet. Telecommunication companies, therefore, play a strategic role in the operation of the Internet.

15. ISP are [*sic*] the commercial entities who provide consumers with access to the Internet. Additionally, ISPs perform other services such as creation of web sites, protocols for selling merchandise, means of direct communication with other web sites, and

related services. ISPs use a variety of telecommunications facilities to operate their portion of the Internet. Some ISPs own their own transmission and packet switching facilities, other purchase or lease [*sic*] transmission and packet switches (routers) while some others simply resell the facilities of other ISPs.

16. Most often, ISPs will lease capacity to connect customers to the Internet. Many ISPs sell "dial-up" service to customers, typically residential customers, travelers or smaller/home offices. To provide this service, the ISP obtains dedicated connections to local exchange carrier central office switches and then advertises its Internet telephone numbers to its subscribers who dial those numbers, reaching a bank of modems that are themselves connected to the ISP's portion of the Internet.

17. While dial up service continues to exist and will likely exist for sometime into the future, consumers have begun to demand, in increasing numbers, digital broadband access to the Internet mainly because the high rate of data transmission is possible with this technology and not possible with dial up technology. DSL service uses conventional voice network to carry digital information by means of a Digital Subscriber Line Access Multiplexer (DSLAM) placed in the central office and a modem placed at the end-users office or home. With a DSLAM at one end of the traditional copper telephone loop and a modem at the other end, it is possible to send bits of data at very high rates of speed. Under conservative network conditions, the commercial deployment of DSL provides a downstream rate of 1.5Mb/s and an upstream rate of approximately 500Kb/s which is

enormously faster (about 5000% in reception and 1700% in transmission) compared to dial up service.

18. For decades, local telephone companies, including defendant SBC (formerly known as Pacific Bell), have owned and controlled facilities that are essential to the provision of many telecommunication services, including DSL service. In most cases, local telephone companies, including defendant SBC, own and control the connections to all or substantially all end user customers. ISPs such as plaintiffs and other similarly situated [*sic*], that are not affiliated with the incumbent local phone company (SBC) must obtain access to those customers [*sic*] connections in order to reach and serve their own end user customers. Additionally, such non affiliated providers often need to interconnect their own facilities with those of the incumbent if they are to be able to provide communications service on a broad scale. Because of the critical nature of the telephone companies' network facilities, they are often referred to as "essential" or "bottleneck" facilities. This is especially true of the "last-mile" connection between the incumbent local telephone company (SBC) central offices and the end-users' premises. Because SBC is both an ISP (PBI) and because SBC/SBC-ASI own and control the essential or bottleneck facilities without which DSL cannot be provided, the ISPs, including plaintiffs, find themselves in direct competition with the supplier of DSL services. Because DSL transmission over the local loop is a bottleneck, defendants have undue influence over the commercial viability of the ISP providers who must purchase DSL service to provide broadband access to their customers. While there are discrete locations where ISPs have a choice of DSL providers, this is rare, because the majority of

such wholesale DSL providers have ceased to operate in any significant geographical region of California; and SBC-ASI enjoys virtually exclusive control over DSL transport in SBC's service area which covers approximately 78% of the geographic area of California. As a consequence, the local telephone company monopolies in California, including defendant SBC, account for approximately 80% of the DSL lines that were installed in California as of March 2001. As the independent ISP/DSL providers continue to decline, the percentage held by the incumbent-monopoly local telephone companies, including SBC, the largest in California, will continue to increase.

19. It is defendants' exercise of this bottleneck power and the imposition of onerous conditions on its rival ISP DSL wholesale customers that is the gravamen of this Complaint. The SBC entities offer DSL services in both retail and wholesale markets. As a result, defendants determine the cost of the critical components of these competitor ISPs' service offerings. Because PBI combines DSL with both online services and equipment (e.g., free modem), which PBI provides as bundled package to end use [*sic*] customers, and because PBI has taken in excess of 80% of the DSL market, independent ISPs are under competitive pressure to meet defendants' prices and service combinations in the marketplace. When the wholesale-retail margin is set artificially low (a price squeeze), the ISPs are placed at a serious unfair disadvantage vis-a-vis the vertically integrated SBC entities.

20. The business of providing Internet access and related services directly affects the flow of telephone service in interstate commerce because the local exchange service is the originating or terminal point

for interstate telephone and data transmission services. Accordingly, the violations of the antitrust laws set forth herein directly and adversely affect and operate to substantially restrain competition in the flow of interstate commerce.

IV.

COUNT ONE

(VIOLATION OF SECTION 2 OF THE SHERMAN ACT)

21. Plaintiffs incorporate by reference the allegations in paragraphs 1 through 20 as though fully set forth herein.

22. Beginning as early as mid-1998 and continuing up to the filing of this Complaint, defendants, the SBC entities, acting as a single entity have monopolized and attempted to monopolize, in violation of Section 2 of The Sherman Act (15 U.S.C. § 2), the relevant markets for providing DSL and other Internet services and local telecommunication services in those various geographic boundaries in the State of California where SBC is authorized to provide local exchange services.

23. In furtherance of its monopolization or attempt to monopolize in violation of Section 2 of the Sherman Act, defendants have done, inter alia, the following acts and practices, all calculated to preserve and maintain its preexisting DSL/ISP and local telecommunication service monopolies and to exclude and unreasonably impede competition from independent ISPs, such as plaintiffs:

(a) created a price squeeze by charging ISP a high wholesale price in relation to the price at which defendants were providing retail services;

(b) intentionally adopted anticompetitive procedures and processes for handling customer ordering and installation to ISPs that are calculated to (i) cause ISP customer disruption and interruption in service, and (ii) create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to defendants;

(c) purposefully created and imposed procedures that impeded, and/or caused significant delays and costs for, end user customers of defendant switching to the services of independent ISPs, including plaintiffs;

(d) misled, harassed and exhibited hostility toward customers of ISPs, including plaintiffs;

(e) disparaged and created doubts about the efficacy and legality of ISPs, including plaintiffs; and

(f) purposefully failed to bill properly for DSL services.

In short, defendants adopted procedures carefully calculated to deny ISPs access to an essential facility and to preserve and maintain its monopoly control of DSL access to the Internet.

V.

EFFECTS OF THE VIOLATION

24. The aforesaid conduct of defendants has produced and, unless restrained by this Court, will continue to produce the following anticompetitive effects among others:

(a) competition in the provision of DSL service has been effectively eliminated and defendants have been able to maintain a monopoly of DSL in its enfranchised service areas in California; and

(b) competition in the provision of Internet services has been effectively eliminated in defendants' California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products.

VI.

INJURY TO PLAINTIFFS

25. As a direct and proximate result of the violations alleged herein, plaintiffs are being, and will continue to be, immediately and irreparably injured in this business and property. Plaintiffs have no adequate remedy at law to compensate for such injury, and unless defendants are restrained by an appropriate order of this Court, plaintiffs will continue to suffer an inability to compete fully and fairly in the relevant markets described herein, will lose substantial goodwill and reputation normally attached to a profitable enterprise and will suffer reduction in the value of their respective businesses as ongoing concerns.

26. As a direct and proximate result of the violations alleged herein and as intended by defendants, each plaintiff has sustained injury to the businesses and properties as follows:

(a) each has sustained a reduction in the number of customers and reduction in its revenues and net profits; and

(b) each has sustained a reduction in the value of its business as a going entity.

Each Plaintiff is each unable, at this time, to quantify with precision the extent of its damages, but estimates the amount to be in excess of Forty Million Dollars ($40,000,000).

VII.

COUNT TWO

(INTENTIONAL INTERFERENCE WITH PROSPECTIVE ECONOMIC ADVANTAGE)

27. Count Two of this Complaint is based on the doctrine of supplemental jurisdiction because the claim asserted herein arises from the same transactions and from a common nucleus of operative facts as alleged in Count One.

28. Plaintiffs incorporate by reference the allegations in paragraphs 2 through 26, inclusive, of this Complaint with the same force and effect as though alleged in full herein.

29. Each plaintiff has had, for many years, and now has valuable and reasonable expectations of business relationships from both existing and prospective customers.

30. Defendants knew or should have known of these business relationships between each plaintiff and its actual and prospective customers and of each plaintiff's reasonable expectations of continued or prospective business relationships with such existing and potential customers. With the intent of disrupting and destroying those business relationships, defendants intentionally and maliciously performed the wrongful acts described in Count One of this Complaint.

31. Defendants have disrupted and continues [*sic*] to disrupt and interfere intentionally with each plaintiff's existing and prospective business relationships as described above in Count One.

32. Plaintiffs incorporate by reference the allegations in Count One of this Complaint in respect to the effect of defendants' conduct and the injury proxi-

mately caused and inflicted on each of them with the same force and effect as though alleged in full herein.

33. The aforesaid acts of interference and disruption were done by defendants knowingly, willfully and maliciously and with intent to injure and oppress plaintiff. Therefore, each plaintiff is entitled to recover exemplary and punitive damages.

VIII.

COUNT THREE

(UNFAIR TRADE PRACTICES)

34. Count Three of this Complaint is based on the doctrine of supplemental jurisdiction because the claim asserted herein arises from the same transactions and from a common nucleus of operative facts as alleged in Counts One and Two.

35. Each plaintiff incorporates by reference the allegations in paragraphs 2 through 26 and 29 through 33, inclusive of this Complaint with the same force and effect as though alleged in full herein.

36. Count Three of this Complaint is filed and these proceedings are instituted against defendants pursuant to Section 17203 of the California Business & Professions Code to obtain restitution and injunctive relief against defendants for their violations of Section 17200 of the California Business & Professions Code and to prevent threatened injury resulting from further violations of said unfair competition laws.

37. Defendants have competed unfairly against plaintiffs as alleged herein and have maintained and diverted customers who otherwise would have migrated to plaintiffs.

38. Such conduct by defendants has been made for the purpose and with the effect of injuring ISPs in general, including plaintiffs, and to thereby destroy

and unreasonably impede competition generally in the provision of ISP/DSL services.

39. Defendants have, by the conduct herein described, violated Section 17200 of the California Business & Professions Code and have been unjustly enriched as a result of such violations.

PRAYER

WHEREFORE, each plaintiff demands judgment against each defendant as follows:

1. On Count One for treble its actual damages, costs, reasonable attorneys' fee, and injunctive relief for violation by each defendant of Section 2 of the Sherman Act (15 U.S C. § 2);

2. On Count Two for compensatory and exemplary damages against each defendant for its intentional interference with plaintiffs' prospective economic advantage;

3. On Count Three for restitution and injunctive relief against each defendant for its violations of Section 17200 of the California Business & Professions Code;

4. For costs and such other and further relief as may be just and proper.

Dated: July 23, 2003

BLECHER & COLLINS, P.C.
MAXWELL M. BLECHER
GARY M. JOYE

By /s/ MAXWELL M. BLECHER
MAXWELL M. BLECHER
Attorneys for PLAINTIFFS

DEMAND FOR JURY TRIAL

Plaintiffs hereby demand a trial by jury pursuant to the Federal Rules of Civil Procedure, Rule 38(b) (28 U.S.C., Rule 38 and Local Rule 38-1).

Dated: July 23, 2003

BLECHER & COLLINS, P.C.
MAXWELL M. BLECHER
GARY M. JOYE

By /s/ MAXWELL M. BLECHER
MAXWELL M. BLECHER
Attorneys for PLAINTIFFS

[Attorney Name/Address
Blocks Omitted]

UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
WESTERN DIVISION

No. CV 03-5265 SVW (SHx)

LINKLINE COMMUNICATIONS, INC., ET AL.,
Plaintiffs,

v.

SBC CALIFORNIA, INC., ET AL.,
Defendants.

FIRST AMENDED COMPLAINT FOR DAMAGES AND INJUNCTIVE RELIEF FOR VIOLATIONS OF ANTITRUST LAWS AND STATE LAW CLAIMS (DEMAND FOR JURY TRIAL)

[Filed December 7, 2004]

The above-named plaintiffs herein file this Complaint for damages and injunctive relief, and, demanding trial by jury, complain and allege as follows:

I.

JURISDICTION AND VENUE

1. This Complaint is filed and these proceedings are instituted against the above-named defendants under Sections 4 and 16 of the Clayton Act (15 U.S.C. §§ 15, 26, respectively) to recover treble damages from and secure injunctive relief against the above-

named defendants for their violations of federal antitrust laws. This Court has original jurisdiction over this federal antitrust claim pursuant to 28 U.S.C. § 1337.

2. Both plaintiffs and defendants transact business, maintain offices and may be found within the Central District of California. The interstate trade and commerce involved and affected by the alleged violations of the antitrust laws was carried on, in part, within this District and some of the unlawful acts described herein were conceived, performed or made effective within this District.

II.

THE PARTIES

3. Plaintiff linkLINE COMMUNICATIONS, INC. ("linkLine") is a corporation organized and existing under the laws of the State of Delaware with its principal place of business in Ontario, California. linkLine is an Internet service provider ("ISP") which provides access to the Internet and related services.

4. Plaintiff InReach Internet LLC ("InReach") is a corporation organized and existing under the laws of the State of California with its principal place of business in Stockton, California. InReach is an ISP which provides access to the Internet and related services.

5. Plaintiff Om NETWORKS, d/b/a OMSOFT TECHNOLOGIES, INC. ("Omsoft") is a corporation organized and existing under the laws of the State of California with its principal place of business in Davis, California. Omsoft is an ISP which provides access to the Internet and related services.

6. Plaintiff NITELOG, INC., d/b/a RED SHIFT INTERNET SERVICES ("Red Shift") is a corporation

organized and existing under the laws of the State of California with its principal place of business in Monterey, California. Red Shift is an ISP which provides access to the Internet and related services.

7. Defendant SBC California, Inc. ("SBC") (formerly known as Pacific Bell Telephone Company or "PacBell") is a corporation organized and existing under the laws of the State of California with its principal place of business in San Ramon, California. SBC has authority to operate as a Local Exchange Carrier ("LEC"), providing local telephone services to California consumers within PacBell's local service area. SBC is a subsidiary of SBC Communications, Inc. On September 17, 1998, SBC received approval from the California Public Utilities Commission ("CPUC"), in Resolution T-16191, to provide Digital Subscriber Line ("DSL") services to California consumers.

8. Defendant Pacific Bell Internet Services ("PBI") is a corporation organized and existing under the laws of the State of California with its principal place of business in San Ramon, California. PBI is a subsidiary of SBC. Consumers who ordered SBC's DSL and chose PBI as their ISP were billed the associated fee for Internet access on their regular monthly Pacific Bell telephone billing statement under the heading "Pacific Bell Internet Services."

9. Defendant SBC Advanced Solutions, Inc. ("SBC-ASI") is a Delaware organized [*sic*] and existing under the laws of the State of Delaware corporation [*sic*], with its principal place of business in Houston, Texas. SBC-ASI is a subsidiary of SBC Communications, Inc., and an affiliate of SBC. In June 2000, responsibility for provisioning and billing of DSL was transitioned from SBC to SBC-ASI. The CPUC granted SBC-ASI a certificate of public

convenience and necessity to operate as a facilities-based provider of competitive local exchange and intraLATA interexchange services. SBC-ASI has since and now provides DSL and other advanced services to independent ISP and California consumers.

10. Defendants SBC, PBI, and SBC-ASI are sometimes collectively referred to as the "SBC entities" or "defendants."

III.

NATURE OF TRADE AND COMMERCE AND RELEVANT MARKETS

11. One of the relevant markets in this case is the market for Digital Subscriber Lines in [*sic*] ("DSL") SBC's telecommunication service region in California, which encompasses the vast majority of the State of California's residential and business users. DSL is distinguished from other means of connecting to the Internet because it is (a) faster, (b) "always on," (c) more reliable, and (d) allows many users in the same geographic area simultaneous access without affecting the speed or quality of the transmission. DSL is also distinguishable in that it can be made available over existing telephone lines which today connect virtually all businesses and households in California. There is a discrete and separate market for DSL because of its distinct characteristics, pricing points and separate and distinct customer demand.

12. Another relevant market in this case is the market for Internet services in SBC's California service region. Users of the Internet demand and rely upon ISPs to provide them with access to the Internet and emails for the creation of home page web sites, advertising, means of selling and collecting from purchasers and other related services which

make the Internet commercially useful. Another relevant market is switched local exchange telecommunications service in SBC's California service region. SBC, the incumbent local exchange carrier, has held and holds monopoly power in that local service market, which it has used to dominate DSL and Internet service markets in California, by its monopoly control and manipulation of essential "bottleneck" local telephone network facilities (including the "last mile" connection to end users premises) through which local telecommunication services are provided, including DSL-Internet services, and which cannot practically or reasonably be duplicated.

13. The Internet allows users to access an almost unlimited amount of information in a manner and speed that was previously unavailable. Moreover, the Internet allows groups and individuals to discover and then interact with one another on the basis of common interest. The Internet has transformed the way research is conducted, the way commerce is transacted and the means of buying and selling. In order for all segments of society to make full use of the Internet resources, there must be affordable access to the Internet.

14. Telecommunications companies as a group provide the backbone and distribution plant for Internet transmission and the gateway by which users access the Internet. Telecommunication companies, therefore, play a strategic role in the operation of the Internet.

15. ISP are [*sic*] the commercial entities who provide consumers with access to the Internet. Additionally, ISPs perform other services such as creation of web sites, protocols for selling merchandise, means of direct communication with other web sites, and

related services. ISPs use a variety of telecommunications facilities to operate their portion of the Internet. Some ISPs own their own transmission and packet switching facilities, others purchase or lease transmission and packet switches (routers) while some others simply resell the facilities of other ISPs.

16. Most often, ISPs will lease capacity to connect customers to the Internet. Many ISPs sell "dial-up" service to customers, typically residential customers, travelers or smaller/home offices. To provide this service, the ISP obtains dedicated connections to local exchange carrier central office switches and then advertises its Internet telephone numbers to its subscribers who dial those numbers, reaching a bank of modems that are themselves connected to the ISP's portion of the Internet.

17. While dial up service continues to exist and will likely exist for sometime into the future, consumers have begun to demand, in increasing numbers, digital high-speed access to the Internet mainly because the high rate of data transmission is possible with this technology and not possible with dial up technology. DSL service uses conventional voice network to carry digital information by means of a Digital Subscriber Line Access Multiplexer (DSLAM) placed in the central office and a modem placed at the end-users office or home. With a DSLAM at one end of the traditional copper telephone loop and a modem at the other end, it is possible to send bits of data at very high rates of speed. Under conservative network conditions, the commercial deployment of DSL provides a downstream rate of 1.5Mb/s and an upstream rate of approximately 500Kb/s which is

enormously faster (about 5000% in reception and 1700% in transmission) compared to dial up service.

18. For decades, local telephone companies, including defendant SBC (formerly known as Pacific Bell), have owned and controlled facilities that are essential to the provision of many telecommunications services, including DSL service. In most cases, local telephone companies, including defendant SBC, own and control the connections to all or substantially all end user customers. ISPs such as plaintiffs and others similarly situated, that are not affiliated with the incumbent local phone company (SBC) must obtain access to those customers' connections in order to reach and serve their own end user customers. Additionally, such non affiliated providers often need to interconnect their own facilities with those of the incumbent if they are to be able to provide communications service on a broad scale. Because of the critical nature of the telephone companies' network facilities, they are often referred to as "essential" or "bottleneck" facilities. This is especially true of the "last-mile" connection between the incumbent local telephone company (SBC) central offices and the end-users' premises.

IV.

GRAVAMEN OF MONOPOLY CLAIM: DEFENDANTS DSL MONOPOLIZATION BY INTENTIONALLY PRICE SQUEEZING THEIR WHOLESALE CUSTOMERS-RETAIL COMPETITORS

19. Because SBC is both an ISP (PBI) and because SBC/SBC-ASI own and control the essential or bottleneck facilities without which DSL cannot be provided, the ISPs, including plaintiffs, find themselves in direct competition at retail with their wholesale

supplier of DSL services upon which they depend to provide DSL service. Because DSL transmission over the local loop is a bottleneck and defendants have monopoly control over the wholesale supply of DSL to ISPs with whom they also compete at retail, defendants have undue influence over the commercial viability of the ISP providers who must purchase DSL service from defendants to provide high-speed Internet access to their customers. While there are discrete locations where ISPs have a choice of DSL providers, this is rare, because the majority of such wholesale DSL providers have ceased to operate in any significant geographical region of California. SBC-ASI enjoys virtually exclusive control over DSL transport in SBC's service area which covers approximately 78% of the geographic area of California and possesses and has manipulated (including through price squeezing conduct alleged below) their monopoly control of the wholesale supply of DSL to ISPs seeking to compete at retail with defendants. As a consequence, the local telephone company monopolies in California, including defendant SBC, account for approximately 80% of the DSL lines that were installed in California as of March 2001. As the independent ISP/DSL providers continue to decline, the percentage held by the incumbent-monopoly local telephone companies, including SBC, the largest in California, will continue to increase.

20. It is defendants' unlawful exercise of this bottleneck monopoly power over the wholesale supply of DSL inputs by imposition of onerous exclusionary conditions on its rival ISP DSL wholesale customers (such as plaintiffs) that compete against defendants at retail – including purposeful price squeezing by charging plaintiffs artificially high wholesale prices

in relation low [*sic*] retail prices charged by defendants to end users – that is the gravamen of this Complaint. The SBC entities offer DSL services in both retail and wholesale markets and have taken unlawful, anticompetitive advantage of rival ISPs (plaintiffs here) status as both a wholesale customer and retail competitor of defendants. Defendants determine the cost of the critical essential components of these competitor ISPs' service offerings which depend upon defendants wholesale supply of DSL. Because PBI combines DSL with both online services and equipment (e.g., free modem), which PBI provides as bundled package to end use [*sic*] customers, and because PBI has taken in excess of 80% of the DSL market, independent ISPs are under competitive pressure to meet defendants' prices and service combinations in the marketplace. When as here the monopolist wholesale prices are set too high relative to its low retail prices – indeed, here for period of substantial time defendants wholesale DSL transport prices charged to independent ISPs actually exceeded the retail price defendants charged end-users for providing a bundle package of DSL-Internet service and necessary equipment – independent ISPs are placed in a price squeeze that puts them at a seriously unfair disadvantage vis-a-vis the vertically integrated SBC monopoly entities and rendering those independent ISPs such as plaintiffs unable to compete with SBC defendants in the retail market for DSL service.

21. Considering defendants unlawful wholesale-retail price squeezing conduct in the context of the totality of various other anticompetitive exclusionary acts directed at ISPs (including anticompetitive provisioning procedures, service disruptions, dis-

paragement, misrepresentations, improper billing) defendants price squeezing conduct was intended to achieve monopolistic purpose of impeding and excluding competition and thereby preserving and maintaining their monopoly over DSL/ISP and local telecommunications service.

22. The business of providing Internet access and related services directly affects the flow of telephone service in interstate commerce because the local exchange service is the originating or terminal point for interstate telephone and data transmission services. Accordingly, the violations of the antitrust laws set forth herein directly and adversely affect and operate to substantially restrain competition in the flow of interstate commerce.

V.

COUNT ONE

(VIOLATION OF SECTION 2 OF THE SHERMAN ACT-MONOPOLIZATION THROUGH PRICE SQUEEZE)

23. Plaintiffs incorporate by reference the allegations in paragraphs 1 through 22 as though fully set forth herein.

24. Beginning as early as mid-1998 and continuing up to the filing of this Complaint, defendants, the SBC entities, acting as a single entity have monopolized and attempted to monopolize, in violation of Section 2 of the Sherman Act (15 U.S.C. § 2), the relevant markets for providing DSL and other Internet services and local telecommunications services in those various geographic boundaries in the State of California where SBC is authorized to provide local exchange services.

25. In furtherance of its monopolization or attempt to monopolize in violation of Section 2 of the Sherman

Act, defendants have done, inter alia, the following acts and practices, all calculated to preserve and maintain their DSL/ISP and local telecommunication service monopolies and to exclude and unreasonably impede competition from independent ISPs, such as plaintiffs:

(A) Intentional Price Squeezing of Wholesale Customers-Retail Competitors:

(1) As set forth above defendants unlawfully manipulated their dual role as vertically integrated monopolists as both a wholesale-monopoly supplier and retail competitor of plaintiffs for DSL by engaging in a unlawful [*sic*] price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services and necessary equipment to end-user customers – and for a period by charging wholesale DSL prices to competing ISPs (such as plaintiffs) that actually exceeded the prices at which defendants retail affiliate (PBI) was charging retail end-user customers for DSL services and necessary equipment – thereby making it impossible for independent ISP competitors such as plaintiffs to compete at the low retail prices set by defendants for combined DSL-Internet Service and necessary equipment provided to end-user customers.

(2) If plaintiffs charged retail DSL-Internet access customers the same retail price as defendants' retail affiliate charged, plaintiffs could not cover the cost of providing DSL service, which costs necessarily includes the wholesale transport costs charged by defendants.

(3) By the same token, if defendants themselves charged their retail affiliates the same wholesale costs for DSL transport that they charged their wholesale ISP customers (such as plaintiffs), defendants could not cover their wholesale costs and make a profit from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation), that were in some cases, and for some period, even below the wholesale DSL transport cost. Given the price margin relationship between retail and wholesale prices, defendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as plaintiffs that are both wholesale customers and retail rivals.

(B) Additional Unlawful, Anticompetitive Acts Demonstrating Specific Intent To Monopolize Through Price Squeeze

In addition to this purposeful price squeezing conduct, defendants also engaged in a course of unfair and unlawful anticompetitive acts and practices directed at their ISP rivals, such as plaintiffs, all calculated to preserve and maintain their DSL/ISP and local telecommunications service monopolies and to exclude and unreasonably impede competition from independent ISPs, such as plaintiffs, including:

(1) intentionally adopted anticompetitive procedures and processes for handling customer ordering and installation to ISPs that are calculated to (i) cause ISP customer disruption

and interruption in service, and (ii) create extraordinary and serious delays and a substantial backlog of orders, in the hope that the ISP customers will revert back to defendants;

(2) purposefully created and imposed procedures and costs that impeded, and/or caused significant delays and costs for, end user customers of defendant switching to the services of independent ISPs, including plaintiffs, and imposed unreasonable and anticompetitive costs of DSL aggregation-backhaul circuits necessary for providing DSL service and particularly given the delays in processing orders, unfairly raised the per-customer costs of independent ISPs trying to compete with defendants.

(3) misled, harassed and exhibited hostility toward customers of ISPs, including plaintiffs;

(4) disparaged and created doubts about the efficacy and legality of ISPs, including plaintiffs; and

(5) purposefully failed to bill properly for DSL services.

In short, defendants engaged in unlawful price squeezing and additional anticompetitive acts and practices carefully calculated to stifle and hinder competition from independent ISPs such as plaintiffs to preserve and maintain its monopoly control of DSL access to the Internet.

VI.

EFFECTS OF THE VIOLATION

26. The aforesaid conduct of defendants has produced and, unless restrained by this Court, will continue to produce the following anticompetitive effects among others:

(a) competition in the provision of DSL service has been effectively eliminated and defendants have been able to maintain a monopoly of DSL in its enfranchised service areas in California; and

(b) competition in the provision of Internet services has been effectively eliminated in defendants' California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products.

VII.

INJURY TO PLAINTIFFS

27. As a direct and proximate result of the violations alleged herein, plaintiffs are being, and will continue to be, immediately and irreparably injured in this business and property. Plaintiffs have no adequate remedy at law to compensate for such injury, and unless defendants are restrained by an appropriate order of this Court, plaintiffs will continue to suffer an inability to compete fully and fairly in the relevant markets described herein, will lose substantial goodwill and reputation normally attached to a profitable enterprise and will suffer reduction in the value of their respective businesses as ongoing concerns.

28. As a direct and proximate result of the violations alleged herein and as intended by defendants, each plaintiff has sustained injury to the businesses and properties as follows:

(a) each has sustained a reduction in the number of customers and reduction in its revenues and net profits; and

(b) each has sustained a reduction in the value of its business as a going entity.

Each Plaintiff is each unable, at this time, to quantify with precision the extent of its damages, but estimates the amount to be in excess of Forty Million Dollars ($40,000,000).

VIII.

COUNT TWO

(INTENTIONAL INTERFERENCE WITH PROSPECTIVE ECONOMIC ADVANTAGE)

29. Count Two of this Complaint is based on the doctrine of supplemental jurisdiction because the claim asserted herein arises from the same transactions and from a common nucleus of operative facts as alleged in Count One.

30. Plaintiffs incorporate by reference the allegations in paragraphs 2 through 28, inclusive, of this Complaint with the same force and effect as though alleged in full herein.

31. Each plaintiff has had, for many years, and now has valuable and reasonable expectations of business relationships from both existing and prospective customers.

32. Defendants knew or should have known of these business relationships between each plaintiff and its actual and prospective customers and of each plaintiff's reasonable expectations of continued or prospective business relationships with such existing and potential customers. With the intent of disrupting and destroying those business relationships, defendants intentionally and maliciously performed the wrongful acts described in Count One of this Complaint.

33. Defendants have disrupted and continues [*sic*] to disrupt and interfere intentionally with each

plaintiff's existing and prospective business relationships as described above in Count One.

34. Plaintiffs incorporate by reference the allegations in Count One of this Complaint in respect to the effect of defendants' conduct and the injury proximately caused and inflicted on each of them with the same force and effect as though alleged in full herein.

35. The aforesaid acts of interference and disruption were done by defendants knowingly, willfully and maliciously and with intent to injure and oppress plaintiff. Therefore, each plaintiff is entitled to recover exemplary and punitive damages.

IX.

COUNT THREE

(UNFAIR TRADE PRACTICES)

36. Count Three of this Complaint is based on the doctrine of supplemental jurisdiction because the claim asserted herein arises from the same transactions and from a common nucleus of operative facts as alleged in Counts One and Two.

37. Each plaintiff incorporates by reference the allegations in paragraphs 2 through 28 and 31 through 35, inclusive of this Complaint with the same force and effect as though alleged in full herein.

38. Count Three of this Complaint is filed and these proceedings are instituted against defendants pursuant to Section 17203 of the California Business & Professions Code to obtain restitution and injunctive relief against defendants for their violations of Section 17200 of the California Business & Professions Code and to prevent threatened injury resulting from further violations of said unfair competition laws.

39. Defendants have competed unfairly against plaintiffs as alleged herein and have maintained

and diverted customers who otherwise would have migrated to plaintiffs.

40. Such conduct by defendants has been made for the purpose and with the effect of injuring ISPs in general, including plaintiffs, and to thereby destroy and unreasonably impede competition generally in the provision of ISP/DSL services

41. Defendants have, by the conduct herein described, violated Section 17200 of the California Business & Professions Code and have been unjustly enriched as a result of such violations.

PRAYER

WHEREFORE, each plaintiff demands judgment against each defendant as follows:

1. On Count One for treble its actual damages, costs, reasonable attorneys' fee, and injunctive relief for violation by each defendant of Section 2 of the Sherman Act (15 U.S.C. § 2);

2. On Count Two for compensatory and exemplary damages against each defendant for its intentional interference with plaintiffs' prospective economic advantage;

3. On Count Three for restitution and injunctive relief against each defendant for its violations of Section 17200 of the California Business & Professions Code;

4. For costs and such other and further relief as may be just and proper.

Dated: December 7, 2004

BLECHER & COLLINS, P.C.
MAXWELL M. BLECHER

By /s/ MAXWELL M. BLECHER
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DEMAND FOR JURY TRIAL

Plaintiffs hereby demand a trial by jury pursuant to the Federal Rules of Civil Procedure, Rule 38(b) (28 U.S.C., Rule 38 and Local Rule 38-1).

Dated: December 7, 2004

BLECHER & COLLINS, P.C.
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PETITIONER'S BRIEF

101

(10)

No. 07-512

FILED
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SUPREME COURT, U.S.

IN THE
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

**On Writ of Certiorari
to the United States Court of Appeals
for the Ninth Circuit**

BRIEF FOR PETITIONERS

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August 28, 2008

QUESTION PRESENTED

Whether a plaintiff states a claim under Section 2 of the Sherman Act by alleging that the defendant – a vertically integrated retail competitor with an alleged monopoly at the wholesale level but no antitrust duty to provide the wholesale input to competitors – engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete.

LIST OF PARTIES TO THE PROCEEDINGS

Petitioners Pacific Bell Telephone Company (which now does business as AT&T California (formerly SBC California)), Pacific Bell Internet Services (now known as SBC Internet Services, Inc. d/b/a AT&T Internet Services and AT&T Entertainment Services), and SBC Advanced Solutions, Inc. (d/b/a AT&T Advanced Solutions) were the defendants in the district court proceedings and the appellants in the court of appeals proceedings.

Respondents linkLine Communications, Inc., In-Reach Internet LLC (now known as InReach Internet, Inc.), Om Networks d/b/a Omsoft Technologies, and Nitelog, Inc. d/b/a Red Shift Internet Services were the plaintiffs in the district court proceedings and the appellees in the court of appeals proceedings.

CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 29.6 of the Rules of this Court, petitioners Pacific Bell Telephone Company (which now does business as AT&T California (formerly SBC California)), Pacific Bell Internet Services (now known as SBC Internet Services, Inc. d/b/a AT&T Internet Services and AT&T Entertainment Services), and SBC Advanced Solutions, Inc. (d/b/a AT&T Advanced Solutions) state the following:

Pacific Bell Telephone Company is a wholly owned subsidiary of AT&T Teleholdings, Inc., which is a wholly owned subsidiary of AT&T Inc. (formerly SBC Communications Inc.). AT&T Inc. has n corporate parent. No publicly held corporation owns 10% or more of the stock of AT&T Inc. AT&T California (formerly SBC California) is the trade name under which Pacific Bell Telephone Company does business in California.

SBC Internet Services, Inc. (formerly Pacific Bell Internet Services) is wholly owned by AT&T Teleholdings, Inc., which is wholly owned by AT&T Inc. SBC Internet Services, Inc. does business under the trade names AT&T Internet Services and AT&T Entertainment Services.

SBC Advanced Solutions, Inc. is jointly owned by AT&T Inc. and AT&T Teleholdings, Inc. SBC Advanced Solutions, Inc. does business under the trade name AT&T Advanced Solutions.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-24a) is reported at 503 F.3d 876. The orders of the district court (Pet. App. 25a-57a, 58a-91a) are not reported.

JURISDICTION

The court of appeals entered its judgment on September 11, 2007. The petition for a writ of certiorari was filed on October 17, 2007, and was granted on June 23, 2008 (128 S. Ct. 2957). The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

Section 2 of the Sherman Act, 15 U.S.C. § 2, provides:

> Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.

STATEMENT OF THE CASE

Respondents (plaintiffs below) purchase communications services at wholesale from petitioners (collectively, "AT&T") and use them to provide retail Internet-access service in competition with AT&T. Respondents alleged that AT&T was a monopolist at the wholesale level and had violated Section 2 of the Sherman Act by creating a "price squeeze." Specifically, respondents alleged that AT&T left an "artificially low" margin between the wholesale price AT&T charged respondents for communications services and the retail prices AT&T charged for Internet-access service, placing respondents at an "unfair disadvantage." Compl. ¶ 19 (JA17).

The Ninth Circuit acknowledged that, under this Court's decision in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), AT&T had no antitrust duty to offer the wholesale input to competitors. Nevertheless, the court found that, because "price squeeze theory form[s] part of the fabric of traditional antitrust law," Pet. App. 14a, respondents had stated a claim.

The Ninth Circuit's decision misreads *Trinko*, which holds that a monopolist has no Section 2 duty to cooperate with a rival in the absence of an affirmative duty to deal under the antitrust laws. That holding necessarily extends to the price at which a monopolist makes a wholesale input available to its competitors. Moreover, the price-squeeze theory approved by the Ninth Circuit – which has no support in this Court's decisions – penalizes pro-competitive conduct and threatens liability in the absence of consumer harm. The decision is thus inconsistent with the most basic canon of this Court's antitrust jurisprudence: that the Sherman Act protects *competition*, not *competitors*. The Court should reverse.

A. Regulatory Background

Under Federal Communications Commission ("FCC") regulations adopted in the 1980s, a Bell Operating Company ("BOC") that wanted to provide computer-related services over its telephone network was required also to provide any underlying communications services to unaffiliated competitors on a nondiscriminatory, common-carrier basis.[1] The FCC indicated that this obligation applied to Internet-access services in general and, in particular, to high-speed Internet-access service provided over digital subscriber lines ("DSL").[2] (In *Brand X*, this Court upheld an FCC determination that cable companies – which provide high-speed Internet-access service over cable lines in competition with telephone companies' DSL service – are not subject to analogous obligations to provide the underlying transmission capacity to unaffiliated Internet-access providers. *See* 545 U.S. at 975, 986-1003.)

In the late 1990s, AT&T's BOC affiliate, petitioner Pacific Bell Telephone Company ("Pacific Bell"), began offering retail high-speed Internet-access service, using DSL technology. Pacific Bell also introduced – as it was required to do – tariffed offerings for "DSL Transport," the wholesale "underlying communications service" that is one component of DSL-based

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[1] *See generally National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 975-77, 992-95 (2005); Report and Order, *Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, 104 F.C.C.2d 958, 964, ¶ 4 (1986). *See also* Pet. App. 78a-84a (describing history of FCC regulations in this area.

[2] *See* Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 17 FCC Rcd 3019, 3031, ¶ 22 (2002).

Internet-access service. *See* Pet. App. 84a. Unaffiliated Internet Service Providers ("ISPs") could purchase DSL Transport from Pacific Bell and then combine it with other facilities and services to provide Internet-access service to retail customers in competition with Pacific Bell and others. *See id.* at 60a.

Subsequently, AT&T modified the structure of its subsidiaries so that defendant SBC Advanced Solutions, Inc. ("SBC-ASI") provided DSL Transport to defendant Pacific Bell Internet Services ("PBIS") and to unaffiliated ISPs. PBIS (rather than Pacific Bell) provided Internet-access service to retail customers. The FCC required SBC-ASI, under this new structure, to provide DSL Transport to unaffiliated ISPs on the same terms and conditions as it provided the service to affiliates.[3] Hence, throughout the period covered by the complaint, AT&T's affiliates' offering of DSL Transport to unaffiliated ISPs has been compelled by and pursuant to FCC regulations.[4]

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[3] *See* Memorandum Opinion and Order, *Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services*, 17 FCC Rcd 27000, 27006-07, ¶ 11, 27009, ¶ 15 (2002).

[4] The FCC has eliminated the obligation of many local telephone companies to provide DSL Transport as a condition of provision of DSL-based Internet-access service. *See* Report and Order and Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853 (2005), *petitions for review denied, Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205 (3d Cir. 2007). In so doing, the FCC noted that "[t]here are numerous technologies and network designs that form, or potentially could form, part of the broadband telecommunications infrastructure of the 21st century," including cable modem service, which accounted for more than 60 percent of residential high-speed Internet connections at the end of 2004. *Id.* at 14873, ¶ 33; *see id.* at 14881-82.

In addition, because DSL Transport is offered as a common-carrier communications service, it is subject to regulation under Title II of the Communications Act of 1934, 47 U.S.C. § 201 *et seq.* The Act requires that "[a]ll charges, practices, classifications, and regulations for and in connection with [interstate] communication service, shall be just and reasonable." *Id.* § 201(b). The Act also forbids "any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communication service." *Id.* § 202(a).

B. District Court Proceedings

1. Respondents are ISPs that "provide[] access to the Internet and related services." Compl. ¶¶ 3-6 (JA11-12). In July 2003, they filed a complaint against petitioners Pacific Bell, PBIS, and SBC-ASI, accusing them of "monopoliz[ing] and attempt[ing] to monopolize . . . the relevant markets for providing DSL and other Internet services and local telecommunication services" in areas of California where AT&T is authorized to provide local service. *Id.* ¶ 22 (JA18). Respondents alleged that, "to exclude and unreasonably impede competition from independent

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¶ 51; *see also Brand X*, 545 U.S. at 1001 (quoting FCC finding that "'[r]esidential high-speed access to the Internet is evolving over multiple electronic platforms, including wireline, cable, terrestrial wireless and satellite'").

As a condition of its recent merger with BellSouth, however, AT&T remains under an obligation to continue to provide the service, at a price no higher than the retail rate AT&T charges for retail DSL-based Internet-access service. *See* Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, 22 FCC Rcd 5662, 5814-15, App. F (2007), *on partial reconsideration on other grounds*, 22 FCC Rcd 6285 (2007).

ISPs," petitioners had "created a price squeeze by charging ISP[s] a high wholesale price in relation to the price at which defendants were providing retail services." *Id.* ¶ 23(a) (JA18). In addition, respondents alleged that petitioners "adopted procedures carefully calculated to deny ISPs access to an essential facility and to preserve and maintain its monopoly control of DSL access to the Internet." *Id.* ¶ 23 (JA19). The complaint makes no mention of competing high-speed Internet-access platforms such as cable modem and wireless technologies.

After this Court decided *Trinko*, AT&T moved for judgment on the pleadings, *see* Fed. R. Civ. P. 12(c), asserting that AT&T had provided DSL Transport to rival providers of retail Internet-access service only under FCC compulsion; that AT&T had no *antitrust* duty to deal with respondents at all; and that respondents' complaints about the terms of dealing between petitioners and respondents therefore failed to state a claim under Section 2. *Cf. Trinko*, 540 U.S. at 409-10.

2. The district court agreed that the bulk of respondents' allegations failed to state a claim and could not proceed. *See* Pet. App. 77a-86a. The court, however, refused to dismiss the price-squeeze claim. The court stated that *Trinko* "simply does not involve price-squeeze claims" and rejected the argument that "a price-squeeze claim essentially boils down to a claim that Firm One is refusing to deal with Firm Two on Firm Two's price terms." *Id.* at 86a. The court found that price-squeeze claims arise in narrower circumstances than other refusal-to-deal claims, because they are limited to circumstances where a firm "operates both as a retailer and a wholesaler whose customers are also its competitors." *Id.* at 87a

(internal quotation marks omitted). The court also stated that, "to the extent that price-squeeze claims are subject to the requirements set forth in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), then the transmutability of refusal-to-deal claims is limited still more." *Id.*

The district court also found that the Ninth Circuit in *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992), had already "rejected the argument that the existence of a regulatory structure precludes antitrust liability under a price squeeze theory." Pet. App. 88a. In addition, the court noted that, "while the *Trinko* Court justified its decision not to expand the scope of Section 2 liability by reference to the existence of a regulatory structure designed to deter and remedy anticompetitive conduct, it justified its conclusion that Trinko's allegations failed to state a claim under existing antitrust standards by reference to existing case law." *Id.* at 90a. "And here, unlike the plaintiff's refusal-to-deal claim in *Trinko*, Plaintiffs' price-squeezing claim falls within the range of recognized Section 2 claims." *Id.*

3. As ordered by the district court, respondents amended their complaint to elaborate their price-squeeze claim. The amended complaint alleges that "defendants unlawfully manipulated their dual role" as a "wholesale-monopoly supplier and retail competitor" by "intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services . . . thereby making it impossible for independent ISP competitors . . . to compete at the low retail prices set by defendants." Am. Compl. ¶ 25(A)(1) (JA35).

The amended complaint further alleges that "for a period" AT&T had "charg[ed] wholesale DSL [Transport] prices . . . that actually exceeded the prices at which [AT&T] . . . was charging retail end-user customers." *Id.* Respondents alleged that, if they charged the same price for Internet-access service as AT&T, they "could not cover the cost of providing" that retail service and that, if AT&T "charged [its] retail affiliates the same wholesale costs for DSL transport that [it] charged [its] wholesale . . . customers . . . , defendants could not cover their wholesale costs and make a profit." *Id.* ¶ 25(A)(2)-(3) (JA35-36). The amended complaint charges that "defendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent" providers of Internet-access service. *Id.* ¶ 25(A)(3) (JA36).

4. AT&T again moved to dismiss, arguing that the claim could proceed only if plaintiffs alleged facts supporting the two prerequisites for a predatory-pricing claim under *Brooke Group* – that is, pricing of the retail Internet-access service below cost and a likelihood of recoupment. The district court acknowledged that there was "persuasive appeal to Defendants' argument that the underlying logic of *Trinko*, which is that no inference of anticompetitive intent can be drawn from a refusal to deal where the parties are compelled by law to deal, applies with equal force to price squeeze claims." Pet. App. 55a. The court nevertheless denied the motion to dismiss. Though "inclined to apply the *Brooke Group* requirements to Plaintiffs' price squeeze claim," the court "conclude[d] that it need not and should not resolve this difficult

issue" because, "even if the *Brooke Group* requirements were applied, the [amended complaint] would satisfy those requirements." *Id.* at 47a-48a.[5]

The district court granted petitioners' motion to certify for interlocutory appeal its order denying petitioners' motion to dismiss. *See id.* at 56a-57a.[6] The Ninth Circuit granted interlocutory review. *See id.* at 92a.

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[5] In reaching this conclusion, the district court applied the now-overruled pleading standard of *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957), *overruled by Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1969 (2007). *See* Pet. App. 49a.

[6] As the government noted in its brief in support of the petition, there is some ambiguity about whether the district court intended to certify both the earlier (October 2004) order and its subsequent (April 2005) order on the amended complaint or whether it intended to certify only the October 2004 order. *See* U.S. Cert. Br. 18-19. The Ninth Circuit evidently believed that the amended complaint was before it. *See* Pet. App. 5a-8a (quoting allegations of the amended complaint). In either event, the district court's certification properly placed before the Ninth Circuit the question presented by AT&T's petition – whether plaintiffs' allegation that defendants engaged in a price squeeze stated a claim under the Sherman Act. The amended complaint includes more detailed factual allegations, but the substance of the price-squeeze allegation in the amended complaint is the same. Those more detailed allegations can supply one version of facts that plaintiffs may posit in defending their claim by illustrating what they think they could have proved under the initial complaint – and this Court may so consider the amended complaint for that purpose. *See Twombly*, 127 S. Ct. at 1969 (noting that, "once a claim for relief has been stated, a plaintiff receives the benefit of imagination, so long as the hypotheses are consistent with the complaint") (internal quotation marks omitted).

C. The Ninth Circuit's Opinion

A divided Ninth Circuit panel affirmed. The majority stated that, "[i]n antitrust terms, a price squeeze occurs 'when a vertically integrated company sets its prices or rates at the first (or "upstream") level so high that its customers cannot compete with it in the second-level (or "downstream") market.'" Pet. App. 8a (citation omitted). The court stated that, "[f]or over six decades, federal courts have recognized price squeeze allegations as stating valid claims under the Sherman Act." *Id.* at 8a-9a (citing, *inter alia*, *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 437-38 (2d Cir. 1945) ("*Alcoa*")). The court also noted its prior holding that "claims of price squeezing under § 2 are viable against monopolists in regulated industries." *Id.* at 9a (citing *City of Anaheim*).

The court acknowledged *Trinko*'s holding that "failure by a monopolist to deal with a competitor on certain service terms when that monopolist was under no duty to deal with the plaintiff . . . did not state a claim under § 2 of the Sherman Act." *Id.* at 9a-10a. It stated that *Trinko* thus "raised the question of whether a price squeeze is merely another term of the deal governed by the Supreme Court's analysis in *Trinko*, or whether it is something else." *Id.* at 10a. Stating that the circuits were already in conflict over the question, *see id.* (comparing *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050 (11th Cir. 2004) (allowing a "price squeezing" claim to proceed), *cert. denied*, 544 U.S. 904 (2005), with *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673-74 (D.C. Cir. 2005) (rejecting price-squeeze claim in the absence of a duty to deal in the

upstream input)),[7] the court concluded that the case before it was controlled by the Ninth Circuit's earlier decision in *City of Anaheim*, which recognized potential price-squeeze claims.

The majority offered two reasons for its decision. *First*, it stated that "*Trinko* did not involve a price squeezing theory" and that, "[b]ecause a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." Pet. App. 14a. *Second*, the court determined that the standard established in *City of Anaheim* was appropriately circumscribed by the requirement that a plaintiff alleging a price squeeze in a regulated industry show "specific intent on the part of the wholesale monopoly holder to 'serve its monopolistic purposes at [retail competitors'] expense.'" *Id.* (quoting *City of Anaheim*, 955 F.2d at 1378) (alteration in original).

The court also stated that "the existence of regulation does not always eliminate the danger of anticompetitive harm." *Id.* at 15a. "The key, under *Trinko*, is the nature of the regulatory structure at issue." *Id.* The court found itself "confronted with a partially regulated industry": while, "[a]t the wholesale level, there are a series of regulatory mecha-

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[7] In fact, the Ninth Circuit's suggestion that there was an existing circuit split was mistaken. As AT&T had explained to the Ninth Circuit, what the Eleventh Circuit referred to as "price squeezing" was in substance a claim for predatory pricing under this Court's test in *Brooke Group*. *See Covad v. BellSouth*, 374 F.3d at 1049-52; *see also Covad Communications Co. v. Bell Atlantic Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005) (order on denial of rehearing) (noting that, in *Covad v. BellSouth*, "the complaint alleged the 'basic prerequisites for . . . price predation'") (quoting 374 F.3d at 1050) (alteration in original).

nisms and regulatory agencies charged with assuring fair play," *id.* at 16a, there is "no comparable regulatory attention paid to the retail DSL market," *id.* at 18a. "It is unclear at this juncture the extent to which linkLine is basing its § 2 price squeezing theory on wholesale pricing, retail pricing, or both. However, since linkLine could prove facts . . . that involve only unregulated behavior at the retail level," its claim could not be dismissed on the pleadings. *Id.*[8]

Judge Gould dissented. In his view, *Trinko* "takes the issues of wholesale pricing out of the case"; to state a claim under Section 2, therefore, plaintiffs would have to allege the elements of a predatory-pricing claim with respect to "retail sales of internet connection[s]." *Id.* at 20a-21a. Under this standard, the amended complaint failed to state a claim: "plaintiffs . . . did not allege that the seller had the market power to set prices for internet connection[s] in the retail market, that [petitioners'] retail price, contributing to the squeeze, was set below cost, and that losses could later be recouped." *Id.* at 23a.

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[8] The Ninth Circuit directed the district court to assess the viability of the claim at summary judgment based on "whether the complained of behavior took place at the regulated wholesale level, the unregulated retail level, or some combination of the two, and to what extent, if any, the responsible agencies have devoted attention to or had involvement in the complained of conduct." Pet. App. 18a.

SUMMARY OF ARGUMENT

Section 2 of the Sherman Act places no obligation on a wholesale monopolist to assist its retail rivals by providing them with a sufficient margin to operate profitably – particularly when the wholesale monopolist has no antitrust duty to deal in the first place.

I. That conclusion follows first from the plain holding of *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004). The plaintiff in that case complained that the defendant failed to provide wholesale network facilities and services to retail competitors in a manner that would allow them to compete effectively in the market for local telephone service. *See id.* at 404-05, 407. This Court held that such an alleged "refusal to cooperate with a rival" could not state a claim under the Court's existing Section 2 precedents where the defendant had no duty, under the antitrust law, to deal with its rival. *See id.* at 408-09. The Court found that no such duty existed where the defendant's dealing had been compelled by regulation and where the wholesale inputs had never been offered voluntarily to non-rivals. *See id.*

Respondents' price-squeeze allegations in this case are indistinguishable in substance from the allegations at issue in *Trinko* and fail for the same reasons. The complaint here alleges that AT&T "created a price squeeze" as one of a series of acts intended to deny respondents access to network facilities allegedly required to compete in the retail Internet-access market. *See* Compl. ¶ 23 (JA18-19). Such an allegation cannot state a claim under Section 2 in the absence of an antitrust duty to provide the facilities in the first place, a duty that does not exist here.

II. The Ninth Circuit majority reasoned that respondents' price-squeeze claim could proceed notwithstanding *Trinko* because such a claim "'satisf[ies] established antitrust standards.'" Pet. App. 14a (quoting *Trinko*, 540 U.S. at 406). But this Court has never recognized "price squeeze" as an independent antitrust tort. *Cf. Trinko*, 540 U.S. at 410-11 (noting that the Court has never recognized lower courts' "essential facilities" doctrine). To the contrary, the hallmark of a price squeeze – the reduction or elimination of the margin between a vertically integrated producer's wholesale and retail prices and resulting reduction in retail competitors' profits – speaks solely to the impact of conduct on *competitors*, not on *competition*, as a process for promoting economic efficiency. Such a doctrinal focus is at odds with the core principle that the Sherman Act was "enacted for the protection of *competition* not *competitors*." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (internal quotation marks omitted).

A. That a price squeeze may eliminate rivals' margins does not mean that it harms *competition* in the relevant sense. *See Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 23 (1st Cir. 1990) (Breyer, J.). "Even when a monopolist at one essential stage 'monopolizes' a second stage, consumer harm cannot be inferred and is difficult to identify." 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 756b, at 11 (2d ed. 2002). For that reason, this Court has held that Section 2 does not condemn "monopoly leveraging" – even when the use of monopoly power allows the defendant to gain a dominant position in a second market – in the absence of conduct that is

otherwise subject to condemnation under Section 2. *Trinko*, 540 U.S. at 415 n.4.

B. A rule treating the existence of a price squeeze as sufficient to state a claim under Section 2 would risk deterring conduct that provides immediate benefit to consumers and enhances efficiency. First, by basing liability on the absence of a sufficient margin between wholesale and retail prices, the doctrine discourages retail price cuts that provide concrete benefits to consumers. *See Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 223-24 (1993). Second, the doctrine would deter efficient voluntary dealing – or vertical integration into downstream markets – by wholesale monopolists now threatened with the burden of protecting the welfare of downstream competitor-customers. Third, as with imposition of duties to deal, recognition of price-squeeze claims would reduce incentives for innovation and investment.

C. The inquiry that "price squeeze" claims require "burdens courts with the prohibitive administrative task of administering the monopolist's prices." 3A Areeda & Hovenkamp ¶ 767d2, at 132. Courts and juries would be required to supervise prices at not one but two levels, "a role for which they are ill suited." *Trinko*, 540 U.S. at 408. Moreover, the possibility that a price squeeze reflects competitive behavior and superior efficiency means that "false condemnations" of benign price squeezes would "'chill the very conduct the antitrust laws are designed to protect.'" *Id.* at 414 (quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986)).

D. On top of all the foregoing reasons, allowing a price-squeeze theory of liability to proceed is particularly inappropriate in circumstances where

the wholesale monopolist has no duty to deal under the antitrust laws. In such circumstances, from the point of view of antitrust law, the wholesale monopolist is free to refuse to deal at all – even if downstream rivals are unable to compete without such assistance – and there is no incremental harm to consumers from arriving at the same result gradually through a price squeeze.

III. Stretching the antitrust laws to encompass a potential price-squeeze claim is particularly unwarranted because "a regulatory structure" already exists "to deter and remedy anticompetitive harm." *Trinko*, 540 U.S. at 412. The FCC has, for nearly four decades, actively policed the provision of information services by communications companies, modifying the scope of regulatory duties-to-deal with unaffiliated information-service providers in response to changing market conditions. *See National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 1001 (2005). The FCC has authority to address price-squeeze allegations that are said to violate regulatory obligations. *Cf. FPC v. Conway Corp.*, 426 U.S. 271 (1976). In light of this regulatory oversight, "the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny." *Trinko*, 540 U.S. at 412.

ARGUMENT

I. *TRINKO* GOVERNS RESPONDENTS' PRICE-SQUEEZE CLAIM AND MANDATES DISMISSAL

Respondents' price-squeeze claim fails first of all because it is barred by *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004). There, this Court held that allegations that a monopoly supplier provided wholesale inputs in a manner that impeded wholesale customers' efforts to compete in downstream retail markets failed to state a claim under Section 2, at least in the absence of an affirmative duty to deal under the antitrust laws. That holding applies to respondents' claim that the price of DSL Transport was too high relative to the price that AT&T charged for DSL-based Internet-access service to allow respondents' to compete successfully.

The factual allegations of respondents' complaint and the complaint in *Trinko* are indistinguishable. In both cases, the gravamen of the complaint was that the defendant had manipulated its role as both a wholesale supplier and a retail competitor to place its wholesale customers at a relative disadvantage in the provision of retail service.

In *Trinko*, the plaintiff alleged that the defendant had "use[d] its control over the physical wires over which phone services are delivered . . . to hinder efforts by [new entrants] to enter into the business of providing local telephone service, while providing adequate services to customers using [the defendant] for their local phone service." Compl. ¶ 1 (*Trinko*

JA12).[9] Claiming that "[a]ccess to [the defendant's] wires is essential for the provision of local telephone service," the plaintiff alleged that the defendant "has deterred and will continue to deter potential customers from switching to another company for local telephone service or cause customers that had switched [to another company for local telephone service] to switch back." *Id.* ¶ 2 (*Trinko* JA13). The plaintiff thus alleged that the defendant had "used its monopoly power in the local loop market to gain a competitive advantage in the market for the provision of Local Phone Service," in particular by failing to provide access to the local loop "on a par with its own access." *Id.* ¶¶ 30, 63 (*Trinko* JA18, 29).

Similarly, respondents here alleged that AT&T had a monopoly in the supposed market for DSL Transport (the wholesale input) by virtue of its "control . . . of essential 'bottleneck' local telephone network facilities." Compl. ¶ 12 (JA14); Am. Compl. ¶ 12 (JA29). Respondents further alleged that ISPs "that are not affiliated with the incumbent local phone company . . . must obtain access to those customers['] connections in order to reach and serve their own end user customers." Compl. ¶ 18 (JA16); Am. Compl. ¶ 18 (JA31). "Because DSL transmission over the local loop is a bottleneck, defendants have undue influence over [plaintiffs'] commercial viability" in the provision of retail DSL-based Internet-access service. Compl. ¶ 18 (JA16); *see* Am. Compl. ¶ 19 (JA32). Thus, the alleged "price squeeze" places respondents "at a serious unfair disadvantage vis-a-vis" AT&T. Compl. ¶ 19 (JA17); *see* Am. Compl. ¶ 20 (alleging

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[9] References to "*Trinko* JA__" are to the Joint Appendix filed in *Trinko*, No. 02-682 (U.S. filed May 23, 2003), and in which the cited complaint in *Trinko* is reproduced.

that respondents are "unable to compete with [AT&T] in the retail market for DSL service") (JA33).

In *Trinko*, the Court recognized that, because the retail competitor's ability to compete with the defendant depended on the defendant's affirmative assistance – provision of the necessary wholesale input – such allegations amounted to a claim that the defendant had "refus[ed] to cooperate with rivals." *Trinko*, 540 U.S. at 408. The Court thus asked whether the allegations fell within the narrow "existing exceptions" to the basic rule that firms have no such duty under Section 2. *Id.* The Court concluded that the "alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents." *Id.* at 410.

The district court here reached the same conclusion – that AT&T had no duty to deal with respondents – and that proposition was "not disputed on appeal," Pet. App. 5a n.6. Indeed, because AT&T was "obligated by law to offer their DSL transport facilities to [respondents]," *id.*, there was no basis for any argument that AT&T "voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion," *Trinko*, 540 U.S. at 409.[10] Likewise, there was no allegation that AT&T ever refused to provide to respondents any product

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[10] Respondents argued in the district court that, because the obligation to provide DSL Transport would not apply "if [AT&T] had not voluntarily entered the DSL market," AT&T's "dealings with [respondents] are ultimately the result of [AT&T's] *choice* to enter the DSL market." Pet. App. 84a. As the district court correctly held, however, "a law that says that one must do B if one does A is compulsory even if it leaves open the option of not doing A." *Id.* at 85a.

"that it already sold at retail" to other customers. *Id.* at 410.[11]

Trinko thus establishes that, at least where AT&T has no duty to deal with respondents, it likewise has no duty to deal with them in a manner that would promote their success in the alleged downstream market for DSL-based Internet-access service. That conclusion applies just as plainly to the allegation that AT&T charged too much for DSL Transport as it does to a claim that other terms of AT&T's provision of that wholesale input were inadequate. "Any claim for excessive rates can be couched as a claim for inadequate services and vice versa." *AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 223 (1998). There is no substantive difference between an allegation that, as a result of the *poor quality* of the wholesale input, a plaintiff's retail product was unattractive to consumers relative to the defendant's retail product at the price the plaintiff could profitably charge and an allegation that, as a result of the *high price* of the wholesale input, a plaintiff's retail product was unattractive to consumers relative to the defendant's retail product at the price the plaintiff could profitably charge. In both cases, the allegation is that the defendant has taken advantage of its control over the wholesale input to make its customer-

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[11] In opposing certiorari, respondents argued that the alleged price squeeze "is akin to . . . the refusals to sell to competitors at retail prices for services 'otherwise marketed or available to the public.'" Cert. Opp. 26. But, as respondents acknowledged, what AT&T sells to retail customers is something different – DSL-based Internet-access service – not the DSL transmission capacity it sells to respondents. *See id.* at 8; *see also* Compl. ¶¶ 11 (alleging "relevant market[] . . . for Digital Subscriber Lines"), 12 (alleging "[a]nother relevant market . . . for Internet services") (JA13); *supra* p. 3; U.S. Cert. Br. 9 n.4.

competitor's downstream product unattractive in comparison to its own. *See* U.S. Cert. Br. 9 ("[R]espondents' price-squeeze allegations amount to nothing more than a claim that petitioners refused to deal on terms that respondents desired.").

The Ninth Circuit's conclusion that *Trinko* did not apply to respondents' price-squeeze claim, *see* Pet. App. 14a, is incorrect.

II. RECOGNITION OF PRICE SQUEEZE AS AN INDEPENDENT ANTITRUST TORT CONFLICTS WITH THIS COURT'S PRECEDENT

The Ninth Circuit went on to hold that respondents' price-squeeze claim could proceed because "price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*." Pet. App. 14a; *see also id.* at 8a ("For over six decades, federal courts have recognized price squeeze allegations as stating valid claims under the Sherman Act."); Statement of the Federal Trade Commission at 3-4, Re: Petition for a Writ of Certiorari in *Pacific Tel. Co. [sic] d/b/a AT&T California v. linkLine Commns., Inc.* (No. 07-512) (May 2008) ("Price-squeeze claims have long been part of the Section 2 doctrine.") ("FTC Statement") (citation omitted). But this Court has never recognized a price-squeeze theory of antitrust liability. *See* U.S. Cert. Br. 11 ("[T]he price-squeeze theory of antitrust liability has never been recognized by this Court."); *cf. Trinko*, 540 U.S. at 410-11. To the contrary, "[w]hen the defendant has no antitrust duty to deal, price-squeeze allegations that are based solely on the margin between an integrated defendant's wholesale and retail prices cannot be reconciled with this Court's . . . antitrust jurisprudence." U.S. Cert. Br. 11.

This is true for several reasons. First, the basis for price-squeeze liability – that is, the elimination of a margin sufficient to sustain downstream competitors – raises no inference of harm to competition. Second, recognition of price-squeeze claims would deter conduct that benefits consumers. Third, because price-squeeze doctrine would saddle courts with prohibitive administrative burdens, any potential competitive impact from a price squeeze "'should be deemed irremedia[ble] by antitrust law.'" *Trinko*, 540 U.S. at 415 (quoting Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 Antitrust L.J. 841, 853 (1989)) (alteration in original). Finally, all of these conclusions apply with special force where a defendant has no duty to deal.

A. The Existence of a Price Squeeze – Even One That Causes Competitors To Exit the Downstream Market – Does Not Support Any Inference of Harm to Competition

Under the standard articulated by the Ninth Circuit, the touchstone for price-squeeze liability is that a vertically integrated monopolist has set its upstream wholesale price "so high that its customers cannot compete with it" in the downstream retail market. Pet. App. 8a (internal quotation marks omitted). That broad articulation of the price-squeeze standard follows from the Second Circuit's decision in *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) ("*Alcoa*"). There, the Second Circuit imposed liability under Section 2 where a wholesale-level monopolist set its wholesale prices above a "fair price" and its retail prices too

low to allow its downstream competitors to make "a living profit." *Id.* at 437.[12]

Thus articulated, price-squeeze doctrine focuses on the well-being of downstream competitors and is therefore inconsistent with the principle that the antitrust laws "were enacted for the protection of *competition* not *competitors*." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (internal quotation marks omitted). As Judge Posner has explained, this principle means that antitrust law does not seek to preserve "competition as a process of rivalry" for its own sake but "competition as a means of promoting economic efficiency." *Olympia Equip. Leasing Co. v. Western Union Tel. Co.*, 797 F.2d 370, 375 (7th Cir. 1986). "Any rule of price-squeeze liability that threatens liability based on the claim that the difference between a firm's upstream and downstream prices leaves downstream rivals an insufficient profit margin substitutes a rule of competitor welfare for consumer welfare." J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 J. Competition L. & Econ. 279, 294 (2008).

The fact that "a 'one-level' monopolist engaged in a prolonged price squeeze may drive independent competitors out of business and thereby extend its

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[12] The Second Circuit indicated that the mere existence of a price squeeze could constitute "an unlawful exercise of 'Alcoa's' power" in the market for aluminum ingot, even if "it was not part of an attempt to monopolize the 'sheet' market." 148 F.2d at 438. The suggestion that "*exercise*" of monopoly power by charging high prices violates Section 2 is, however, contrary to this Court's understanding that "[t]he mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system." *Trinko*, 540 U.S. at 407.

monopoly power to a second industry level . . . does not mean that a price squeeze is anticompetitive." *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 23 (1st Cir. 1990); *see* 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 756b, at 11 (2d ed. 2002). In a case – like this one – where the wholesale input and the downstream product are in fixed proportion, an upstream monopolist generally cannot earn any greater profits by eliminating an efficient competitor in the downstream market. "The reason is that [the upstream monopolist] Firm 1 already has all the power it needs, by assumption, to extract the profit from [the downstream retail competitor] Firm 2 by raising [the price of the wholesale input] to just enable Firm 2 to earn a normal rate [of] return without driving Firm 2 out of business. Firm 1 gains nothing further by destroying Firm 2." Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct?*, 4 J. Competition L. & Econ. 271, 275 (2008); *Western Res., Inc. v. Surface Transp. Bd.*, 109 F.3d 782, 787 (D.C. Cir. 1997) ("there is only one monopoly profit to be gained from the sale of an end-product or service"); *Town of Concord*, 915 F.2d at 23.[13]

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[13] It has been argued that a benefit of preserving downstream rivals is that it may facilitate those rivals' eventual challenge to the defendant's wholesale monopoly. *See Town of Concord*, 915 F.2d at 24; FTC Statement at 4-5. In this case, of course, there was no allegation that respondents had any intention of challenging AT&T's alleged wholesale monopoly – to the contrary, respondents alleged that the "local telephone network facilities . . . through which local telecommunication services are provided . . . cannot practically or reasonably be duplicated." Compl. ¶ 12 (JA14). In any event, it is inconsistent with recognized limits on the reach of Section 2 to require a monopolist to assist a potential rival by protecting its downstream profits for the (highly speculative) purpose of promoting upstream entry.

Recognizing that "extension" of a monopoly is not in itself anticompetitive, this Court has held that Section 2 does not condemn "monopoly leveraging" – use of monopoly power to gain an advantage in a second market – unless it involves otherwise wrongful conduct. *Trinko*, 540 U.S. at 415 n.4.[14]

Further, any possible anticompetitive consequences stemming from the inability of a second-level rival to remain in the market must be balanced against the likelihood that the retail competitors' inability to compete is the result of desirable efficiencies, from which consumers benefit. As the leading treatise recognizes, the traditional suspicion of "price squeeze" reflects a misplaced concern about vertical integration. *See* 3A Areeda & Hovenkamp ¶ 767c, at 126 ("it is difficult to see any *competitive* significance [of a price squeeze] apart from the consequences of vertical integration itself"). But vertical integration "can produce significant cost reductions" by enabling the integrating firm to achieve both "'[p]roduction' efficiencies" – that is, "savings in the cost of producing or distributing goods" – and "'[t]ransactional' efficiencies" – that is, avoidance of costs associated with dealing with other firms. *Id.* ¶ 757a, at 23. Where this is so, "prices that squeeze the less efficient second-level competitors, even to the point of forcing

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See Trinko, 540 U.S. at 415-16 (noting that duties intended to promote competitive entry are "much more ambitious than the antitrust laws").

[14] In any event, as the dissent below pointed out, the alleged possibility that AT&T might achieve a monopoly in high-speed Internet-access service ignores the reality that AT&T must compete with alternative platforms, including "cable and . . . satellite" as well as wireless networks. Pet. App. 19a-20a; *see supra* note 4.

them from the business, could (by lowering costs) lower prices, or, in any event, save economic resources." *Town of Concord*, 915 F.2d at 24. Moreover, when second-level rivals "exhibit[] some market power," a price squeeze may reflect elimination of supra-competitive margins at the second level. 3A Areeda & Hovenkamp ¶ 756b3, at 14-15. In this situation as well, "price will ordinarily come down and output will ordinarily increase." *Id.*; *see Town of Concord*, 915 F.2d at 24-25.

In sum, the existence of a price squeeze – even if it leads to downstream rivals' exit from the market – provides no sound basis for inferring consumer harm, the concern of antitrust law.

B. Recognition of Price-Squeeze Claims Would Deter Pro-Competitive Conduct

Treating the existence of a price squeeze as the basis for a claim under the antitrust laws is unwarranted for the additional reason that such a rule would discourage pro-competitive conduct.[15] *See generally* David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 81 (2005) ("Barring procompetitive practices is likely to

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[15] Almost by definition, price-squeeze claims are brought by rivals, not by consumers; consumers benefit from the very downstream prices that discomfit rivals. This provides an additional reason to be skeptical about such claims. *See* William J. Baumol & Alan S. Blinder, *Economics: Principles & Policy* 275 (10th ed. 2006) (noting that "[o]ne problem that haunts most antitrust litigation is that vigorous competition may look very similar to acts that *undermine* competition and support monopoly power" and that "effective competition by a firm is always tough on its rivals").

be more costly, on average, than permitting anti-competitive practices.").

First, and most obvious, recognition of price-squeeze claims exerts pressure on a vertically integrated monopolist to keep its downstream retail prices high. *See* Carlton, *Price Squeeze* at 277 (noting that, "[i]f there were a recognized price squeeze theory and the courts subjected firms to it, then [a vertically integrated monopolist] might charge a higher price than necessary for [the downstream product] to avoid any possible litigation"; such higher prices would "lead to consumer harm"); *see also* Sidak, *Abolishing Price Squeeze* at 297 ("[T]he price-squeeze theory of liability . . . permits the misuse of an antitrust doctrine as [a] vehicle for keeping retail prices high.").[16] Even if superior efficiency were a justification for a price squeeze, it would always be difficult for an adjudicator to distinguish a price squeeze resulting from such efficiency from a price squeeze resulting from supposedly excessive wholesale prices. *See Town of Concord*,

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[16] A doctrine that requires a wholesale monopolist to preserve downstream rivals' margins may bring about higher prices in another way – that is, by inducing rivals to coordinate retail prices. Armed with a potential claim under Section 2, a downstream rival is likely to "ask or demand that the monopolist eliminate the squeeze," and the "vertically integrated monopolist faces an incentive to behave like a price fixer" by raising its retail prices in response to the demand. Sidak, *Abolishing Price Squeeze* at 297; Herbert J. Hovenkamp & Erik N. Hovenkamp, *The Viability Of Antitrust Price Squeeze Claims*, Univ. of Iowa Legal Studies Research Paper No. 08-33, at 28 (July 2008) ("[R]ecognition of [price-squeeze] claims, if based on a rule that entitles the smaller firm to a profitable margin, would virtually require price fixing by the two firms."). In this way, recognition of price-squeeze liability "may facilitate the supreme evil of antitrust: collusion." *Trinko*, 540 U.S. at 408.

915 F.2d at 24; Carlton, *Price Squeeze* at 276 ("[T]he inquiry as to whether a price squeeze leads to competitive harm necessarily must be conducted ex post, which therefore makes it impossible for a firm to know in advance whether its pricing practices will be anticompetitive."). The existence of a rule subjecting price squeezes to special antitrust scrutiny could thus discourage aggressive retail pricing, harming consumers. *See Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993) ("discouraging a price cut and . . . depriving consumers of the benefits of lower prices . . . does not constitute sound antitrust policy"); *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990) ("Low prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition.").[17]

Second, subjecting a wholesale monopolist to potential liability for a price squeeze would deter efficient vertical integration and socially desirable, voluntary dealing. A monopolist might offer an upstream product, used by another firm to produce a downstream product. If the monopolist begins to produce the downstream product itself, it might well

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[17] Respondents did not allege, either in the complaint or in the amended complaint, that AT&T engaged in predatory pricing. Neither complaint alleges either pricing below cost or a likelihood of recoupment. A price squeeze – even one involving a wholesale price that exceeds the defendant's retail price – need not involve any below-*cost* pricing. *See* Hovenkamp & Hovenkamp, *Viability Of Price Squeeze* at 20. Thus, there is no "sacrifice[e]" of profits at the retail level, and, in any event, it is nonsensical to allege that AT&T could make up for such a "sacrifice[e]" through increased "margins" on the wholesale side, Am. Compl. ¶ 25(A)(3) (JA36), when the complaint alleges that AT&T is trying to force its wholesale customers out of business.

face the prospect of price-squeeze litigation brought by the current downstream producer. Such a possibility might either deter the monopolist from entering the downstream market (even in cases where it would be more efficient than existing rivals) or deter the monopolist from selling to downstream producers in the first place. *See* Carlton, *Price Squeeze* at 277-78; *cf. Olympia*, 797 F.2d at 375 (if a firm "lay[s] itself open to an antitrust suit" when it deals voluntarily with rivals, it will likely refrain from such dealing). In either case, consumers are harmed.

In fact, the very incidents of vertical integration that yield the greatest consumer benefit – lower-cost production in downstream markets – are precisely those that will "squeeze" downstream competitors. As this Court has remarked with respect to claims of above-cost predatory pricing claims, in many cases "the exclusionary effect [here, of price squeeze] . . . reflects the lower cost structure of the alleged predator, and so represents competition on the merits." *Brooke Group*, 509 U.S. at 223. Hence, a rule that outlaws price squeezes penalizes those instances of vertical integration – and behavior by vertically integrated monopolists – that promise the greatest benefit.

Third, by threatening antitrust liability based in part on allegedly high wholesale prices charged by a lawful monopolist, price-squeeze claims impinge on "an important element of the free-market system," that is, a legitimate monopolist's "opportunity to charge monopoly prices." *Trinko*, 540 U.S. at 407. Allowing such claims to proceed would thus undermine incentives for "innovation and economic growth." *Id.*[18]

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[18] *See* 3A Areeda & Hovenkamp ¶ 767d2, at 133 ("[A] common consequence of [*Alcoa*'s] 'solution' is to confront a monopo-

More generally, forcing a firm to protect its downstream rivals from the possibility of a price squeeze is one way of "[c]ompelling such firms to share the source of their advantage," which may "lessen the incentive for the monopolist, the rival, or both to invest in . . . economically beneficial facilities." *Id.* at 407-08; *see also AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 429 (1999) (Breyer, J., concurring in part and dissenting in part) ("It is in the *un* shared, not in the shared, portions of the enterprise that meaningful competition would likely emerge."); Hovenkamp & Hovenkamp, *Viability Of Price Squeeze* at 5-6 (forcing a wholesale monopolist to maintain a downstream rival's profitability "has the perverse effect of removing that rival's incentive to innovate, as it receives the same returns regardless of any improvements").

C. Price-Squeeze Doctrine Imposes Inappropriate Regulatory Burdens on Antitrust Courts

Recognition of a duty under the antitrust laws to avoid "anticompetitive" price squeezes would also impose inappropriate administrative burdens on antitrust courts, contrary to this Court's antitrust teaching. *Trinko* holds that antitrust laws eschew imposition of duties that would "require[] antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill suited" – or that would

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list with two choices: to forgo monopoly profits or to avoid or abandon partial vertical integration. It is thus inconsistent with either of two other basic legal propositions: that a lawful monopolist is entitled to charge a monopoly price, and that partial vertical integration by a monopolist is presumptively lawful because it is economically beneficial.").

"require continuing supervision of a highly detailed decree." 540 U.S. at 408, 414-15. Yet recognition of price-squeeze claims would require courts to supervise prices at not one but *two* levels – the prices for both wholesale inputs and downstream retail services – and ensure that their interaction did not unduly restrict competitors' ability to compete in the retail market. *See* 3A Areeda & Hovenkamp ¶ 767d2, at 132 (price-squeeze doctrine, as articulated in *Alcoa*, "burdens courts with the prohibitive administrative task of administering the monopolist's prices").

Indeed, the *Alcoa* price-squeeze test invoked by the Ninth Circuit – which makes liability turn on a monopolist's "charg[ing] more than a 'fair price' for the primary product while simultaneously charging so little for the secondary product that its second-level competitors cannot make a 'living profit'" – is famously difficult to administer. *Town of Concord*, 915 F.2d at 25.

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" . . . And how should the court respond when costs or demands change over time, as they inevitably will?

Id.[19]

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[19] *But see* FTC Statement at 4 (arguing that "a profit sufficient for participants in the second market to compete" is "at

Nor is it an answer to this conundrum to require that the monopolist maintain a margin between wholesale and retail prices that reflects its own incremental costs of production.[20] There is no basis in antitrust law for requiring a vertically integrated producer to treat the *price* charged to others for a wholesale input as the *cost* of the input to itself; to the contrary, such a requirement ignores economic reality and would again deprive the producer and consumers of the benefits of vertical integration. *See* 3A Areeda & Hovenkamp ¶ 757a, at 24 ("It is not antitrust's purpose to condemn cost-reducing innovations or structures, even if one consequence is to injure rivals unable to match the cost reductions."). As a lawful monopolist in the wholesale product, an integrated producer is entitled to charge its customers the monopoly price for the wholesale input, but it is equally entitled to ignore the price charged to others and instead to consider the *cost* of producing that input in setting its own retail price. A contrary rule will exacerbate all the substantive ills discussed above, by placing upward pressure on retail prices and discouraging voluntary dealing.[21]

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least as clear as the undefined 'below-cost' standard in *Brooke Group*").

[20] This appears to be the standard that respondents intended to invoke in their amended complaint by alleging that, if AT&T "charged [its] retail affiliates the same wholesale costs for DSL transport that [it] charged [its] wholesale . . . customers . . . , defendants could not cover their wholesale costs and make a profit." Am. Compl. ¶ 25(A)(2)-(3) (JA35-36).

[21] The same observations apply to respondents' allegation that, for some period, AT&T's wholesale prices exceeded its retail prices. *See* Am. Compl. ¶ 20 (JA33).

Furthermore, in the complicated communications marketplace, a comparison of the wholesale prices to any set of "costs"

As one commentator has concluded, "[p]roperly understood, a price squeeze is a regulatory issue, which makes sense only as a rule of price regulation in an industry already subject to duties to deal and to control by institutionally competent regulators." Sidak, *Abolishing Price Squeeze* at 294. "[A]ssessing [price-squeeze] claims requires a court to predict the 'correct' price, and doing so places it in the position of a public utility regulator. That objection was good when Judge Breyer uttered it in 1990 . . . , and it remains so today." Hovenkamp & Hovenkamp, *Viability Of Price Squeeze* at 28. As with claims of above-cost price-predation, therefore, a claim of anticompetitive price squeeze should be treated as "'beyond the practical ability of a judicial tribunal to control.'" *Trinko*, 540 U.S. at 414 (quoting *Brooke Group*, 509 U.S. at 223).

D. Recognition of Price-Squeeze Claims Is Particularly Inappropriate in the Absence of Any Antitrust Duty To Deal

Based on the foregoing considerations, leading economists – including the immediate past chief economist in the Department of Justice Antitrust Division – and legal commentators have concluded that judicial recognition of price squeeze as a theory

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is likely to be both difficult and contentious. By providing Internet-access service, AT&T may acquire sources of revenue that supplement the retail service fee – advertising, sale of additional services, partnerships with other businesses. Thus, a simple comparison between the price of DSL Transport and the basic retail price of Internet-access service says nothing about whether wholesale cost exceeds expected per-subscriber revenue – as the familiar examples of free Internet-access service and free e-mail service illustrate. Moreover, a comparison of static costs and revenues ignores altogether long-term strategic considerations.

of antitrust liability is unwise. *See* Carlton, *Price Squeeze* at 278 ("Using a general theory of price squeeze to create antitrust liability is likely to chill competition and harm consumers."); Sidak, *Abolishing Price Squeeze* at 294 ("It is not possible to advance consumer welfare with an antitrust rule that punishes a firm for failing to ensure its competitors' profitability.").

The question presented here, however, is narrower, because AT&T had no antitrust duty to deal with respondents at all. As a result, the potential antitrust benefit from imposition of a duty to avoid a price squeeze is non-existent. From the point of view of antitrust law, AT&T could have stopped dealing with respondents altogether without incurring any liability. There is no basis for imposing an antitrust duty on a firm to shelter its competitors by avoiding a price squeeze when the firm has no obligation to deal at all. *See* Hovenkamp & Hovenkamp, *Viability Of Price Squeeze* at 14 ("[a]ssuming that the refusal to deal and 'instant' termination of the smaller firm were legal to begin with, . . . it is difficult to see how" an alleged price squeeze could cause any "incremental consumer harm").

At the same time, all of the undesirable substantive and institutional consequences of recognizing a price-squeeze theory of liability are nonetheless present and some are accentuated. A defendant will face the same disincentive to price aggressively at the retail level; will face a strong disincentive to commence voluntary dealing and diminished incentives to enter downstream markets; and will continue to face a penalty for charging otherwise lawful prices. And courts will continue to confront an intractable problem of direct price administration.

This is why the D.C. Circuit and the "leading treatise" have recognized that "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673-74 (D.C. Cir. 2005) (quoting 3A Areeda & Hovenkamp ¶ 767c5, at 129-30). This Court should endorse that view and reverse the Ninth Circuit's decision.

III. THE EXISTENCE OF REGULATORY OVERSIGHT PROVIDES AN ADDITIONAL REASON TO DISMISS THE COMPLAINT

The regulatory context in which respondents' claim arises provides an additional reason not to stretch Section 2 to reach the alleged conduct.

"'[A]ntitrust analysis must sensitively recognize and reflect the distinctive economic and legal setting of the regulated industry to which it applies.'" *Trinko*, 540 U.S. at 411 (quoting *Town of Concord*, 915 F.2d at 22). The FCC has been actively involved for nearly four decades in the regulation of computer-related services provided over communications networks. *See* Pet. App. 78a-84a (describing history of FCC regulation of provision of "enhanced services" by telecommunications companies); *see also National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 975-77 (2005). The FCC first adopted various regulations designed to afford unaffiliated providers of computer-related services access to local telephone companies' networks on terms that would seek to eliminate telephone companies' natural advantages over unaffiliated providers. Over time, the FCC has eased those regulations in various respects, and in recent years – in light of increased competition among facilities-based providers of Internet-access

service – it has eliminated many pre-existing restrictions. Throughout that period, the expert regulator has had the opportunity to calibrate regulatory obligations in response to changing market conditions. *See Brand X*, 545 U.S. at 1001.

With respect to the pricing issues implicated in this case, the FCC has the authority to enforce statutory requirements that the rates AT&T charges for interstate telecommunications services – including the rate for DSL Transport – be "just and reasonable," 47 U.S.C. § 201(b), and not unreasonably discriminatory, *id.* § 202(a). The Ninth Circuit observed that AT&T's retail Internet-access prices are not subject to direct regulatory control, *see* Pet. App. 18a, but the FCC's deliberate choice not to regulate downstream retail prices does not mean that respondents had no opportunity to bring the alleged price squeeze at issue here to regulators' attention. To the contrary, it has always been open to respondents to argue that AT&T's wholesale prices are unlawful in light of AT&T's retail prices. *Cf. FPC v. Conway Corp.*, 426 U.S. 271, 277-79 (1976) (holding that Federal Power Commission had authority to consider relationship of jurisdictional and non-jurisdictional rates in determining whether jurisdictional rates were just, reasonable, and nondiscriminatory).

The FCC's existing regulations therefore provided a "regulatory structure" designed "to deter and remedy" any "anticompetitive harm" that might arise from the sort of price squeeze alleged here. *Trinko*, 540 U.S. at 412. "Where such a structure exists, the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny." *Id.*

Following on the panel majority's observation regarding the absence of direct regulation of retail prices, respondents have argued that a price-squeeze claim should be permitted here because AT&T is regulated "'at only one level'" and may be "'seek[ing] to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first.'" Cert. Opp. 32 (quoting *Town of Concord*, 915 F.2d at 29). But this argument fails for at least three reasons. First, respondents have not alleged facts that would support any such theory in this case; to the contrary, respondents alleged that AT&T intends to make up for a reduction in margins *at the unregulated retail level* by charging more at the *regulated* wholesale level. *See* Am. Compl. ¶ 25(A)(3) (JA36). Second, as explained above, because the FCC has authority to take retail rates into account in assessing rates charged at the wholesale level, the FCC could address any such supposed "regulatory avoidance" directly. Third, and most fundamentally, the task of enforcing regulatory obligations is one for regulators, not for antitrust courts. *See Trinko*, 540 U.S. at 406-07, 415-16; *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128, 136-37 (1998). Thus, while respondents argue that "the existence of sharing duties" under FCC regulations "supports [their] case," this Court should reject that argument here as it did in *Trinko*. 540 U.S. at 411.

CONCLUSION

The judgment of the court of appeals should be reversed and the case remanded with instructions to dismiss the complaint.

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August 28, 2008

RESPONDENT'S BRIEF

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No. 07-512

IN THE

Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
d/b/a AT&T CALIFORNIA, *et al.*,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,

Respondents.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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CORPORATE DISCLOSURE STATEMENT

Respondent linkLine Communications, Inc., has no corporate parent and no publicly held corporation owns more than 10% of its stock.

Respondent Nitelog, Inc., has no corporate parent and no publicly held corporation owns more than 10% of its stock.

Respondent In-Reach Internet, LLC (now known as InReach Internet, Inc.) has a corporate parent named MobilePro Corp., a publicly held corporation; and In-Reach Internet, LLC, has assigned to its former corporate parent Balco Holdings, Inc., a California corporation, its rights with respect to this litigation subject to retention by MobilePro Corp. of consent and rights to receive a portion of any proceeds from this litigation as set forth in that assignment agreement dated as of October 31, 2005, by and among In-Reach Internet, LLC, InReach Internet, Inc., Balco Holdings Inc; and no publicly held corporation owns more than 10% of the stock of Balco Holdings, Inc., but MobilePro Corp. is a publicly held corporation that owns, and is the corporate parent of, InReach Internet, Inc., the successor of the original named Plaintiff In-Reach Internet, LLC.

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STATEMENT OF THE CASE

A. Background

Respondents (plaintiffs below) are four Internet Service Providers (ISPs). Pet. App. 2a-3a. They provide Internet access, including via Digital Subscriber Line ("DSL") service, and related services to retail customers, in competition with petitioners. *Id.* Unlike facilities-based local telephone companies (such as petitioners), respondents do not own or control the transmission lines to connect their customers to the Internet. *Id.* Instead, they require access to petitioners' local phone facilities, including local telephone lines, for such connections, which respondents leased from petitioners on a wholesale basis under "a DSL transport" service. *Id.*

Petitioners (SBC entities, now AT&T) were organized so that they sold wholesale DSL access to independent ISPs and sold retail DSL Internet access through their retail affiliate to individual consumers. *Id.* at 3a. Petitioners supplied respondents at wholesale the necessary input (DSL transport) to their DSL service; and petitioners in turn competed with respondents in providing a retail bundled DSL Internet access service (incorporating DSL transport service, along with equipment, activation and online services). *Id.* at 2a-3a; *see also* J.A. 17 (¶ 19). Petitioners were required by federal telecommunications law to offer respondents their DSL transport service on a nondiscriminatory basis. Pet. App. 5a n.6.

B. District Court Proceedings

1. Initial Complaint and 2004 Order

In July 2003, respondents filed their complaint against petitioners, alleging they monopolized and attempted to monopolize the relevant regional DSL Internet service market in violation of Section 2 of the Sherman Act (15 U.S.C. § 2). Pet. App. 4a; J.A. 18-20 (¶¶ 22-24).[1] Respondents' complaint alleged that, "to exclude and unreasonably impede competition from independent ISPs," petitioners "created a price squeeze by charging ISP[s] a high wholesale price in relation to the price at which [petitioners] were providing retail services." J.A. 18 (¶ 23).[2] Petitioners' retail affiliate,

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1. Respondents alleged the market for DSL Internet service in petitioners' telecommunication service region in California is a relevant market. J.A. 13 (¶ 11). DSL is distinguishable from other means of connecting to the Internet because it is (a) faster, (b) "always on," (c) more reliable, and (d) allows many users in the same geographic area simultaneous access without affecting the speed or quality of the transmission. *Id.* DSL service is also distinguishable in that it can be made available over existing telephone lines which today connect virtually all businesses and households in California. *Id.* There is a discrete and separate market for DSL because of its distinct characteristics, pricing points and separate and distinct customers. *Id.*

2. Respondents also alleged petitioners adopted an array of anticompetitive procedures and practices that, taken in conjunction with price squeezing, were "calculated to deny ISPs access to an essential facility and to preserve and maintain [petitioners'] monopoly control of DSL access to the Internet." J.A. 19 (¶ 23(b)-(f)).

which provides a bundled offering of DSL access with both online Internet services and equipment (e.g., free modem), has taken in excess of 80% of the retail DSL market. J.A. 17 (¶ 19).

After this Court's decision in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), petitioners moved for judgment on the pleadings under Fed. R. Civ. P. 12(c) contending that decision compelled judgment in their favor on respondents' complaint. Petitioners asserted they had provided DSL transport service to rival providers of retail Internet access service only under regulatory (FCC) compulsion; that they had no antitrust (as opposed to regulatory) duty to deal; and that respondents' allegations about the terms of compulsory dealings between petitioners and respondents failed to state a claim under Section 2, in light of *Trinko*. Pet. App. 65a-90; *see* J.A. 1 (No. CV 03-5265, No. 16, Notice of Motion and Motion for Judgment on the Pleadings)).

In the October 2004 Order ("2004 Order"), the district court granted petitioners' motion with respect to respondents' non-price squeeze allegations, concluding they were "refusal to deal" and "denial of access to essential facilities" claims barred by *Trinko*. Pet. App. 77a-86a, 90a-91a. But the court denied the motion as to the price squeeze claim, holding that "because a price-squeeze claim is actionable under existing antitrust standards, and because the Ninth Circuit has upheld the viability of price-squeeze claims in the context of highly regulated industries, *Trinko* does not bar [respondents'] price-squeezing claim." *Id.* at 91a; *see id.* at 90a ("And here, unlike the plaintiff's

refusal-to-deal claim in *Trinko*, [respondents'] price-squeezing claim falls within the range of recognized Section 2 claims.").

The court stated "*Trinko* simply does not involve price-squeeze claims" and petitioners' argument that "a price-squeeze claim is essentially a refusal-to-deal claim" – i.e., "claim that Firm One is refusing to deal with Firm Two on Firm Two's price terms" – "does not hold up to sustained scrutiny." *Id.* at 86a-87a. "Moreover, to the extent that price-squeeze claims are subject to the requirements set forth in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), then the transmutability of refusal-to-deal claims is limited still more." *Id.* at 87a.

The district court did not reach petitioners' "objections to the legal sufficiency of [respondents'] price-squeeze claims which [did] not derive from *Trinko*," and ordered respondents "to file with the Court an amended complaint limited to the price-squeeze claim that details beyond the normal requirements of [Fed. R. Civ. P.] 8 specific facts supporting [respondents'] price-squeeze claim." *Id.* at 91a.

2. Amended Complaint and 2005 Order

Respondents filed an amended complaint on their price squeeze claim, alleging that petitioners engaged in an unlawful price squeeze by "intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services and necessary equipment to end-

user customers" and that "for a period by charging wholesale DSL prices to competing ISPs (such as [respondents]) that actually exceeded the prices at which [petitioners'] retail affiliate (PBI) was charging retail end-user customers for DSL [Internet] services and necessary equipment." J.A. 35 (¶ 25(A)(1)). This price squeezing made "it impossible for independent ISPs . . . to compete at the low retail prices set by [petitioners] for combined DSL-Internet Service and necessary equipment." *Id.*

Respondents further alleged that "if [petitioners] themselves charged their retail affiliate[] the same wholesale costs for DSL transport that they charged their wholesale ISP customers," the retail affiliate "could not cover [its] wholesale costs and make a profit from DSL service at [its] low retail prices for [the] bundled offering of DSL, Internet Service and necessary equipment (e.g., free modem and installation)." J.A. 36 (¶ 25(A)(3)). Moreover, "[g]iven the price margin relationship between retail and wholesale prices, [petitioners] are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs. . . ." *Id.* Respondents alleged that petitioners' retail affiliate "has taken in excess of 80% of the [retail] DSL market" (J.A. 33 (¶ 20); and "competition in the provision of Internet service has been effectively eliminated in [petitioners'] California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products" (J.A. 38 (¶ 26(b)).

Petitioners moved to dismiss the price squeeze claim of the amended complaint, arguing (a) price squeeze claims must satisfy the two prerequisites of a predatory pricing under *Brooke Group* – that is, predatory pricing of the retail Internet access service and recoupment – and (b) that the amended complaint failed to do so. Pet. App. 36a. In the April 2005 Order ("2005 Order"), the district court denied that motion. *Id.* at 25a-57a. The court stated that it was "inclined to apply the *Brooke Group* requirements to [respondents'] price squeeze claim," "find[ing] the policy arguments in favor of their application persuasive," but it "[n]evertheless . . . conclude[d] that it need not and should not resolve this difficult issue at this time" noting that "[t]he issue will thus be revisited at summary judgment." *Id.* at 47a-48a & n.15. The court gave two reasons for this. "First, the Court would benefit from further briefing and a fully developed factual record. Second, the Court finds that, even if the *Brooke Group* requirements were applied, the [amended complaint] would satisfy those requirements." *Id.* at 48a.

Then, examining the amended complaint's price squeeze allegations under the *Brooke Group* requirements, the court concluded respondents "can clearly prove a set of facts in support of their price squeeze claim that would entitle them to relief," noting that those allegations "contain[] price squeeze allegations substantially similar to those approved by the [Eleventh Circuit] in [*Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004)]." Pet. App. 48a-49a & n.16; *see id.* at 50a-52a. As the Eleventh Circuit had done in *BellSouth*, the district court addressed the sufficiency of the pleadings on the *Brooke*

Group elements under the "no set of facts" standard (*Conley v. Gibson*, 355 U.S. 41, 45-46 (1957)) that was subsequently repudiated in *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1969 (2007). The court determined that the amended complaint, "generously construed, would state a valid price squeeze claim under *Brooke Group*" and therefore denied the motion to dismiss. Pet. App. 56a.

In its 2005 Order, the district court also granted petitioners' alternative request to amend its earlier 2004 Order regarding *Trinko's* application to certify it for interlocutory appeal pursuant to 28 U.S.C. § 1292(b), identifying the "controlling question of law" as "whether *Trinko* bars price squeeze claims where the parties are compelled to deal under the federal communications laws." *Id.* at 56a-57a.[3] The Ninth Circuit granted interlocutory review. *Id.* at 92a.

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3. The court noted:

> [i]n light of [its] holding that the [amended complaint] can be read to state a viable price squeeze claim under *Brooke Group*, the issue before the Ninth Circuit will not only be whether *Trinko* bars price squeeze claims generally but, more specifically, whether it bars predatory price squeeze claims (i.e., price squeeze claims which comply with the *Brooke Group* requirements).

Id. at 56a n.22.

C. Ninth Circuit Proceedings and Opinion

A divided Ninth Circuit panel affirmed, ruling:

> Based on the record before us at this time, we are able to conclude that the district court was correct to deny the [petitioners'] motion for judgment on the pleadings because [respondent's] allegation that the pricing scheme created an anticompetitive price squeeze states a potentially valid claim under § 2 of the Sherman Act.

Pet. App. 18a-19a. The district court's ruling on the petitioners' "motion for judgment on the pleadings" was in the 2004 Order, which addressed the initial complaint and viability of price squeeze claims under *Trinko* (*Id.* at 53a, 56a-57a), not in the 2005 Order, which addressed the sufficiency of the amended complaint's allegations under *Brooke Group* (*id.* at 36a-52a).

The panel majority decision sets forth the allegations of both the complaint and amended complaint and discusses both the 2004 Order and 2005 Order (*id.* at 5a-8a), and states "[i]t is unclear at this juncture the extent to which [respondents] [are] basing [their] § 2 price squeezing theory on wholesale pricing, retail pricing, or both" (*id.* at 18a). Nevertheless, as the Government has stated in its briefs at the petition stage (U.S. Invitation Brief at 19 n.7) and here (U.S. Merits Brief at 8 n.5): "In the end, . . . [the court of appeals] affirmed the district court's denial of petitioners' 'motion for judgment on the pleadings,' [Pet. App.] at 19a, which was the ruling in the 2004 Order, not the 2005 Order."

In any event, the panel majority did not address the sufficiency of respondents' allegations under *Brooke Group*, or whether respondents' price squeeze claims would need to meet the pleading requirements for a predatory pricing claim under *Brooke Group*. This was apparently because the majority did not believe that these *Brooke Group* issues, addressed in the 2005 Order, were properly before it on the interlocutory appeal. As the Government has stated in its brief on petition and here, "it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal." U.S. Invitation Brief at 20; U.S. Merits Brief at 17.

Petitioners had argued to the court of appeals that "even if *Trinko* did not bar their price squeeze claim, the Court should not reach the *Brooke Group* issue because that issue is not properly before the Court." 05-56023, Docket No. 25, Appellant's Reply Brief at 18 (2/21/06).[4] Petitioners offered three reasons:

> First, as [respondents] acknowledge, although the issue was addressed in the district court's April 2005 order, the district court did not resolve it. It concluded that it need not do so because [respondents] argued (and the

4. Petitioners' argument was responding to respondents' argument that the court of appeals could and should decide whether *Brooke Group* elements were required to state a valid price squeeze claim that would survive *Trinko*, and if they were required, that respondents' amended complaint had sufficiently pled those requirements as the district court had ruled in its 2005 Order. 05-56023, Docket No. 21, Brief of Appellees at 24, 28-31 (1/18/06).

> district court agreed) that, even if *Brooke Group* applies, their [amended] complaint meets its pleading standards [and] . . . also concluded that it would benefit from a more fully developed factual record before finally resolving the issue.

Id. Second, petitioners noted, "the issue was not part of the order the district court certified for interlocutory appeal. The only order certified was the district court's October 2004 order, which was limited to the application of *Trinko* and did not address the *Brooke Group* issue." *Id.* "And, third, [respondents] did not file any cross-petition to bring either the April 2005 order or this issue before this Court." [5] *Id.*

The panel majority seems to have endorsed petitioners' view of what was before it, because it affirmed only on the narrow issue framed by the district court's denial of the "motion for judgment on the pleadings" in the 2004 Order, and not the 2005 Order denying motion to dismiss the amended complaint under *Brooke Group*. Pet. App. 19a. The panel majority decision states "[i]t is unclear at this juncture the extent to which [respondents] [are] basing [their] § 2 price squeezing theory on wholesale pricing, retail pricing,

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5. Petitioners' Opening Brief before the court of appeals noted: "The district court's [2005] [O]rder also addressed whether a price squeeze claim, if it were to survive *Trinko*, would need to meet the pleading requirements for a predatory pricing claim under *Brooke Group*. . . ." but the court "need not address that issue, however, as the price squeeze claim does not survive *Trinko*." 05-56023, Docket No. 14, Appellants' Opening Brief at 12 n.7 (12/5/05).

or both." *Id.* at 18a. "However, since [respondents] could prove facts, consistent with its complaint, that involve only unregulated behavior at the retail level, [their] action or lawsuit survives a motion for judgment on the pleadings." *Id.*[6]

Judge Gould apparently had a different view of what was certified for review – if not necessarily on substantive antitrust law and the implications of *Brooke Group*.[7] In his dissent, Judge Gould concluded that the amended

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6. The panel majority stated:

> We do not preclude the district court, however, from re-examining the viability of this claim on summary judgment after the record is more fully developed and it is clear whether the complained of behavior took place at the regulated wholesale level, the unregulated retail level, or some combination of the two, and to what extent, if any, the responsible agencies have devoted attention to or had involvement in the complained of conduct.

Pet. App. 18a.

7. Days before its decision here, the Ninth Circuit recognized:

> the Court's opinions [in *Brooke Group* and *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 549 U.S. 312 (2007)] strongly suggest that, in the normal case, above-cost pricing will not be considered exclusionary conduct for antitrust purposes, and the Court's reasoning poses a strong caution against condemning bundled discounts that result in prices above a relevant measure of costs.

Cascade Health Solutions v. PeaceHealth, 502 F.3d 895, 912 (9th Cir. Sept. 4, 2007), *amended on other grounds*, 515 F.3d 883, 901 (9th Cir. 2008).

complaint should be dismissed. *Id.* at 19a-24a. Though his dissent does not discuss the 2005 Order's rulings on *Brooke Group*, Judge Gould concluded respondents could not state an antitrust violation for price squeeze without satisfying the predatory pricing requirements of *Brooke Group* with respect to petitioners' pricing in the retail DSL service market, finding the amended complaint deficient in that regard. *Id.* at 22a-23a. He stated "[petitioner's] setting of its sale price of the use of its land lines by ISPs in a wholesale transaction cannot be the basis of an antitrust claim in light of *Trinko*." *Id.* at 22a. "That, however, does not dispose of scrutiny of [petitioner's] conduct in the retail market, for it is the price at which [petitioner] sells DSL service to its retail customers that squeezes [respondents'] ability to resell internet connections at a profit." *Id.* Therefore, "the 'price squeeze' contention boils down to a claim of a predatory pricing on sales of internet connections by [petitioners] in the retail market." *Id.* Judge Gould stated,

> if [respondents] are able to allege that the [petitioners] had market power in the retail market to set or influence the price, and that their retail sales of internet connection were predatory in the sense of being below cost with a real prospect of recoupment, then the case should proceed for factual development.

Id. at 20a-21a.

Judge Gould concluded that the amended complaint did not sufficiently plead the requirements of a Section 2 monopolization claim based on predatory pricing under

Brooke Group. *Id.* at 23a. But he also concluded "it would [not] be correct to dismiss the complaint on the pleadings with prejudice" because "we have not heretofore held that there must be a showing of market power in the retail market, nor held that the standards of *Brooke Group* must be applied in assessing predation in the retail side of a 'price squeeze.'" *Id.* Instead, he recommended, "after dismissal, [respondents] should have been free to amend their complaint if they could assert in good faith the allegations that are requisite here, after *Trinko*." *Id.* at 23a-24a.

Respondents now believe that is a proper disposition of this matter and request that this judgment below be vacated and the case remanded for further proceedings.

SUMMARY OF ARGUMENT

I. Although it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal, it is clear respondents' pricing squeeze claim survives *Trinko* only if it satisfies the requirements of a predatory retail pricing claim under *Brooke Group*. Judge Gould's dissent and the decisions of the only two other circuit courts (the Eleventh Circuit and D.C. Circuit) having addressed the issue recognize that predatory price squeeze claims satisfying the requirements of *Brooke Group* are viable under "'established antitrust standards'" and therefore are not barred by *Trinko*. Petitioners point to no authority or rationale for imposing a *Trinko* bar to a valid *Brooke Group* predatory retail pricing claim along the lines set out in Judge Gould's dissent.

A. Petitioners and their supporting *amici curiae*, notably the Government, argue the panel majority decision erred in recognizing respondents' price squeeze allegations survive *Trinko*, absent an antitrust duty to deal or predatory pricing under *Brooke Group*. U.S. Merits Brief at 9, 29; U.S. Invitation Brief at 13-14, 20-21; Pet. 21-22.[8] Petitioners neither definitively admit nor deny that a *Brooke Group* claim along the lines suggested by Judge Gould's dissent (i.e., predatory pricing at the retail level) survives *Trinko*.[9] In any event, their own cited authority, including Judge Gould's dissent, clearly establish that *Trinko* does not bar a predatory pricing claim under *Brooke Group*. There is no contrary authority suggesting that such a claim would be barred absent an antitrust duty to deal (where dealings are compelled by regulation); and it would be irrational to read *Trinko* as barring a *Brooke Group* claim challenging unregulated retail pricing conduct.

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8. The Government, however, questioned the Court's jurisdiction to decide whether "respondents could avoid dismissal by alleging the elements of a predatory-pricing claim under *Brooke Group*." U.S. Invitation Brief at 20 n.8.

9. *See* Brief of *Amici Curiae* Professors and Scholars in Law and Economics in Support of the Petitioners at 2 ("We agree with Judge Gould's dissent . . . that *Trinko* 'takes the issues of wholesale pricing out of the case,' such that the [respondents'] only possible remaining theory of harm would be predatory pricing at the retail level – which the [respondents] did not allege." (citation omitted)); *see also* Brief for Verizon Communications Inc. and The National Association of Manufacturers as *Amici Curiae* Supporting Petitioners at 22 ("[petitioners'] low retail price is lawful as long as it is not predatory under the demanding standards of *Brooke Group*").

In *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004) ("*BellSouth*"), the court, addressing price squeeze allegations "substantially similar" to those here,[10] held the "[plaintiff's] price squeezing claim survives because it is based on traditional antitrust doctrine and is not specifically barred by *Trinko*," and indeed *Trinko* "'preserves claims that satisfy existing antitrust standards.'" *Id.* at 1050, 1052 (quoting *Trinko*, 540 U.S. at 407).

In *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005) ("*Bell Atlantic*"), the court held that the price squeeze claim there – alleging too high wholesale prices for the provisioning of unbundled loops compelled by new duties imposed under the Telecommunications Act of 1996 – was barred by *Trinko*. *Id.* at 673-74. Yet, as the D.C. Circuit explained in its order on denial of rehearing on that decision, the argument that "the court's holding 'eliminates' the antitrust claim of a price squeeze, simply misreads our opinion." *Covad Communications Co. v. Bell Atlantic Corp.*, 407 F.3d 1220, 1222 (D.C. Cir. 2005). "Notably, the court did not face a circumstance similar to that in *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050-52 (2004), in which the Eleventh Circuit held a claim for predatory pricing of loops could proceed; in that case the complaint alleged the 'basic prerequisites for . . . price predation.'" *Id.*

Judge Gould's dissent also confirmed that while "*Trinko* insulates from antitrust review the setting of the upstream [wholesale] price" (Pet. App. 22a), "if

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10. Pet. App. 49a n.16 (2005 Order).

[respondents] are able to allege that the [petitioners] had market power in the retail market to set or influence the price, and that their retail sales of internet connection were predatory in the sense of being below cost with a real prospect of recoupment, then the case should proceed for factual development" (*id.* at 20a-21a).

B. Recognizing the viability of a predatory retail pricing claim (as set out in Judge Gould's dissent) would not chill competitive pricing, harm consumers, or conflict with any regulatory regime designed to address the antitrust harm of the challenged pricing conduct. Such a claim is directed at unregulated, exclusionary pricing "to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market" (*Brooke Group*, 509 U.S. at 222), depriving consumers of lower prices, better (more diverse) products, and more efficient production methods.

Imposing antitrust liability for such predatory retail pricing would not undermine or override any regulatory regime or structure designed to deter or remedy the anticompetitive harm of that pricing conduct. *Trinko*, 540 U.S. at 411-12 (citing *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 22 (1st Cir. 1990) (Breyer, C.J.)). Here – unlike *Trinko* and *Town of Concord* – the challenged conduct does not arise in the context of a fully regulated industry. Specifically, in the retail DSL market, there has been "no comparable regulatory attention" as on the wholesale side and hence "[a]ny restrictions on pricing at the retail level derive primarily from the antitrust laws." Pet. App. 18a (panel majority opinion). The challenged retail pricing conduct would

implicate the "special problem" that "is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." *Town of Concord*, 915 F.2d at 29 (citing 3 P. Areeda & D. Turner, *Antitrust Law* ¶ 726e, at 217-20 (1978)).

II. Respondents' price squeeze allegations in its amended complaint are, as the district court's 2005 Order noted, "substantially similar" to those that the Eleventh Circuit's *BellSouth* decision found sufficient at the pleading stage to satisfy *Brooke Group* and that were distinguished by, and would survive under, the D.C. Circuit's *Bell Atlantic* decision.[11] Petitioners and the Government correctly note, however, that the district court's 2005 Order ruling that the amended complaint pled a *Brooke Group* predatory pricing claim was decided under the "no set of facts" pleading standard (*Conley*, 355 U.S. at 45-46) that was subsequently repudiated in *Twombly*, 127 S. Ct. at 1969. And they agree with Judge Gould's dissent that the amended complaint does not state a *Brooke Group* claim.

But whether respondents do or can sufficiently plead a predatory pricing claim under *Brooke Group*, particularly in light of *Twombly*, need not and should

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11. As the district court below ruled in denying petitioners' motion to dismiss, "even if the *Brooke Group* requirements were applied, the [amended complaint] would satisfy those requirements," noting it "contains price squeeze allegations substantially similar to those approved by the [Eleventh Circuit] in [*BellSouth*]." Pet. App. 48a-49a & n.16.

not be decided on this interlocutory appeal – and neither petitioners nor the Government suggest it should.[12] As Judge Gould recommended, the proper course is to remand this case back to the district court with instructions that respondents be given leave to amend their complaint to allege, if they can, a valid retail predatory pricing claim under *Brooke Group*.

ARGUMENT

I. *TRINKO* DOES NOT BAR A PREDATORY PRICING CLAIM THAT SATISFIES THE ELEMENTS OF *BROOKE GROUP*

A. A Predatory Pricing Claim Is Viable Under Established Antitrust Standards

As the panel majority decision observed, "*Trinko* took great care to explain that in this particular regulatory context, 'claims that satisfy established antitrust standards' are preserved." Pet. App. 14a

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12. As the Government has stated, "it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal." U.S. Merits Brief at 17. At the petition stage, the Government stated:

> To be sure, the Court might lack jurisdiction to decide the distinct questions whether (a) respondents could avoid dismissal by alleging the elements of a predatory-pricing claim under *Brooke Group*, and (b) whether the amended complaint alleged such a claim, but those questions would not merit this Court's review at this time in any event.

U.S. Invitation Brief at 20 n.8.

(quoting *Trinko*, 540 U.S. at 406). *Trinko* addressed whether the conduct complained of there, involving a defendant's "alleged insufficient assistance in the provision of service to rivals," violated "pre-existing antitrust standards," and concluded it was not "a recognized antitrust claim under this Court's existing refusal-to-deal precedents." *Trinko*, 540 U.S. at 407, 410. Here, as the Eleventh and D.C. Circuits and Judge Gould's dissent have confirmed, predatory pricing claims that satisfy *Brooke Group* satisfy "'established antitrust standards'" and hence are not barred by *Trinko*.

The Government states that here "[a]llegations satisfying the *Brooke Group* requirements with respect to the retail market might suffice," and that such a claim, "to be viable, it would have to satisfy *Brooke Group* by alleging that 'the prices complained of are below an appropriate measure of its rival's costs' and that the defendant had 'a dangerous probability[] of recouping its investment in below-cost prices.'" U.S. Merits Brief at 29 (quoting *Brooke Group*, 509 U.S. at 222, 224; citing Pet. App. 20a-21a (Gould, J., dissenting))[13]; *see also id.* at 9 ("[t]o state a claim based on petitioners' retail prices, respondents would have to allege the two requirements established by this Court for predatory-pricing" under *Brooke Group*).

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13. As the Government notes: "[T]wo other circuits have correctly recognized that *Trinko* and *Brooke Group* combine to bar a margin-based price-squeeze claim. See *Covad Commc'ns Co. v. BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004), cert. denied, 544 U.S. 904 (2005); *Covad Commc'ns Co. v. Bell Atl. Corp.*, 398 F.3d 666, 673-674 (D.C. Cir.), order on denial of reh'g, 407 F.3d 1220, 1222 (D.C. Cir. 2005); see also U.S. Invitation Br. 15-16." U.S. Merits Brief at 29 n.18.

Petitioners too have agreed that

> [a]n integrated retail provider could 'squeeze' rivals by lowering its prices below its costs, but, where that is an antitrust wrong, the rules of predatory pricing – which require a plaintiff to show both below-cost pricing and a likelihood of recoupment of losses, *see Brooke Group*, 509 U.S. at 222, 224 – fully address that behavior. *See* 3A [Phillip E.] Areeda & [Herbert] Hovenkamp ¶ 767c, at 127 [(2d ed. 2002)] (only potential competitive harm from 'price squeeze' should be 'resolved under the law of predatory pricing').

Pet. 21-22; *see also id.* at 3 ("low prices are not unlawful unless predatory pursuant to the standard established in *Brooke Group*"), at 26 ("this Court has adopted for predatory-pricing claims a rule that is clear and administrable").

Neither petitioners nor the Government appear to dispute that a *Brooke Group* claim involving predatory pricing in the retail market would state a viable claim not barred by *Trinko*, so that, as Judge Gould concluded,

> if plaintiffs are able to allege that the [petitioners] had market power in the retail market to set or influence the price, and that their retail sales of internet connection were predatory in the sense of being below cost with a real prospect of recoupment, then the case should proceed for factual development.

Pet. App. 20a-21a.

At the petition stage, the Government questioned whether the Court has jurisdiction to decide the question "whether . . . respondents could avoid dismissal by alleging the elements of a predatory-pricing claim under *Brooke Group*." U.S. Invitation Brief at 20 n.8. But there can be no proper basis for contesting Judge Gould's conclusion that a predatory retail pricing claim satisfying the elements of *Brooke Group* would survive *Trinko;* indeed that conclusion accords with the two circuit court decisions having addressed the question of whether a *Brooke Group* predatory pricing-squeeze claim survives *Trinko.*

B. The Decisions of the Eleventh and D.C. Circuits and Judge Gould's Dissent Confirm *Trinko* Does Not Bar a *Brooke Group* Claim

1. The Eleventh Circuit's decision in *BellSouth* held that the "[plaintiff's] price squeezing claim survives because it is based on traditional antitrust doctrine and is not specifically barred by *Trinko*." 374 F.3d at 1050. *BellSouth* noted that *Trinko* "'preserves claims that satisfy existing antitrust standards'" in rejecting the argument that *Trinko* or the federal telecommunications regulation excluded facially valid predatory price squeeze claims. *Id.* at 1052 (quoting *Trinko*, 540 U.S. at 407). It stated "[o]ur responsibility under *Trinko* to harmonize the Sherman Act and the [Federal Telecommunications Act] does not entail excluding facially valid antitrust claims at the pleadings stage." *Id.*

The Eleventh Circuit determined in *BellSouth* that the plaintiffs' price-squeezing claim must and did "contain allegations that the two basic prerequisites for a showing of price predation under § 2 of the Sherman Act have been met" – that is, (a) "'the prices complained of are below an appropriate measure of its rival's costs'" and (b) "'a dangerous probability[] of recouping its investment in below-cost prices.'" *Id.* at 1050 (quoting *Brooke Group*, 509 U.S. at 222, 224). In determining the plaintiffs there had sufficiently pled those elements, the court relied upon allegations "substantially similar" to those in respondents' amended complaint, as noted in the district court's 2005 Order. Pet. App. 48a-49a & n.16; *id.* Pet. App. 52a.

2. The D.C. Circuit's opinion in *Bell Atlantic* also recognizes that a predatory pricing claim survives *Trinko*. The court's initial opinion held that the price squeeze claim alleging an ILEC's [incumbent local exchange carrier] too high wholesale prices for the provisioning of unbundled loops – a provisioning that was purely the product of "statutory compulsion" – was indistinguishable from and barred by *Trinko*. 398 F.3d at 673. The court then added, "[a]nd, as observed in a leading treatise, 'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Id.* (quoting 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 767c3, at 129-30 (2d ed. 2002)). Petitioners assert that "[t]his Court should endorse that view." Petitioners' Brief at 35. That view and the quoted passage from the "leading treatise" cannot be read to reject predatory pricing claims absent an antitrust duty to deal.

First, as the D.C. Circuit explained in its order on denial of rehearing on that decision, the suggestion that "the court's holding 'eliminates' the antitrust claim of a price squeeze, simply misreads our opinion." *Bell Atlantic*, 407 F.3d at 1222. "Notably, the court did not face a circumstance similar to that in *Covad Communications Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050-52 (2004), in which the Eleventh Circuit held a claim for predatory pricing of loops could proceed; in that case the complaint alleged the 'basic prerequisites for . . . price predation.'" *Id.* "Here, Covad did not argue its claim as one of price predation and, unsurprisingly, we did not treat it as such." *Id.*

Second, as Judge Gould's dissent points out, while *Bell Atlantic* views *Trinko* as "insulat[ing] from antitrust review the setting of the upstream [wholesale] price" that "does not dispose of scrutiny of [petitioner's] conduct in the retail market, for it is the price at which [petitioner] sells DSL service to its retail customers that squeezes [respondents]." Pet. App. 22a. Thus, a properly pled *Brooke Group* claim alleging predatory pricing in that retail market would not be barred by *Trinko*. *Id.* at 20a-21a.

Third, the quoted passage from "the leading treatise" is premised on the assumption that the integrated monopolist "was free to refuse to deal," so the predatory price squeeze conduct could not have harmed competition or consumers any more than a lawful outright refusal to deal. Here, however, the monopolist had a legal duty to deal, albeit based on regulation, and hence could not lawfully refuse to deal with its competitors in the downstream market.

Therefore, predatory pricing accomplishing elimination of competition and monopolization in the downstream market would harm consumer welfare – in the form of higher prices, reduced choice and loss of efficiency and superior services (as alleged here, J.A. 37-38 (¶ 26)) – in a manner that could not have been accomplished by a lawful refusal to deal. *See Town of Concord*, 915 F.2d at 29 (recognizing the "special problem" posed by a price squeezing "monopolist, regulated at only one level, who seeks to dominate a second, unregulated level"); *id.* at 21-22 ("[A] practice is 'anticompetitive' only if it harms the competitive process. It harms that process when it obstructs the achievement of competition's basic goals – lower prices, better products, and more efficient production methods." (citations omitted)). Indeed, the treatise recognizes that "a predatory price squeeze by an integrated monopolist should be unlawful . . . where monopolization of the second stage would be unlawful." 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 767c5, at 130. It also confirms a predatory pricing squeeze can harm competition and therefore "raises a question of unlawful conduct, but that question must be resolved under the law of predatory pricing." *Id.* ¶ 767c, at 127; Pet. at 21-22.

Finally, nothing in *Trinko* or *Brooke Group* suggests that such a predatory pricing claim is barred unless the monopolist had an antitrust duty to deal with the predatory pricing victim.[14] Reading *Trinko* in such a

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14. *See Trinko*, 540 U.S. at 410 ("We conclude that Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's (Cont'd)

manner would confer antitrust immunity for predatory pricing schemes harming consumer welfare where the duty to deal giving rise to competition stems from regulation rather than antitrust. Petitioners, however, have never suggested the regulation giving rise to the duty to deal here, any more than the regulation addressed in *Trinko*, conferred antitrust immunity. Reading *Trinko* to bar predatory pricing claims would put it at odds with *Brooke Group*. And it would allow monopolists to use their regulatory duties to deal in the upstream (wholesale) market to immunize unregulated predatory pricing to eliminate competition in the downstream (retail) market and thereby monopolize that market to the detriment of consumer welfare. As Justice (then Chief Judge) Breyer stated in *Town of Concord*: "We recognize that a special problem is posed by a [price squeezing] monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." 915 F.2d at 29.

Therefore, as Judge Gould's dissent recognized, in line with *BellSouth* and *Bell Atlantic*, a complaint containing allegations sufficient to satisfy the *Brooke Group* requirements with respect to the retail market would be viable and not barred by *Trinko*. Pet. App. 22a-24a.

(Cont'd)

existing refusal-to-deal precedents."); *Brooke Group*, 509 U.S. at 222-26; *id.* at 222 ("the essence of the claim . . . is . . . [a] business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market").

C. Recognition of a *Brooke Group* Claim Along the Lines Suggested by Judge Gould's Dissent Would Not Threaten to Undermine *Trinko* or Fundamental Antitrust Principles

Petitioners and its *amici curiae* argue that recognition of a "price-margin" claim of the type alleged in the initial complaint would undermine *Trinko* and well-settled antitrust doctrine. These arguments are clearly inapplicable to a predatory retail pricing claim satisfying the requirements of *Brooke Group* as discussed in Judge Gould's dissent.[15]

1. Predatory pricing claims that satisfy the requirements of *Brooke Group* are different from those addressed in *Trinko* and "'satisfy established antitrust standards'" and so are preserved under the reasoning of *Trinko*. Recognizing such claims would not impinge on any legitimate element of a "free-market system" or chill legitimate economic growth or innovation, as discussed in *Trinko*; nor would it force an upstream monopolist to uneconomically prop up less efficient downstream rivals to the detriment of consumer welfare. Rather, a *Brooke Group* predatory retail pricing claim of the type discussed in Judge Gould's dissent is directed

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15. It is unclear that these arguments, rebutted here, were directed at a predatory retail pricing claim along the lines Judge Gould set forth; they seem to be directed at "price-margin squeeze" claims only. But petitioners recommend "endors[ing]" the view that "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal'" (setting aside that petitioners here were not "free to refuse to deal"). *Bell Atlantic*, 398 F.3d at 673 (citation omitted). So, caution dictates addressing them in this brief.

at an upstream monopolist's unregulated conduct to eliminate equally efficient competition in a downstream retail market. *See Town of Concord*, 915 F.2d at 29 (recognizing the "special problem . . . posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level"). Such a claim does not chill lawful price cutting or put upward pressure on prices to the detriment of consumers. Rather, it preserves retail competition from equally efficient competitors, and thereby achieves "competition's basic goals" of "lower prices, better products, and more efficient production methods." *Id.* at 22; *see also Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979) ("Congress designed the Sherman Act as a 'consumer welfare prescription'" (citation omitted)).

Indeed, the "essence" of a predatory pricing claim is that a "business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market." *Brooke Group*, 509 U.S. at 222. As stated in *Town of Concord*, as an argument "against permitting extension of monopoly power": "The existence of competitors at a second 'level,' irrespective of their effects upon price, provides an added incentive for the monopolist to develop better products and better, more efficient ways to produce the product." 915 F.2d at 24; *see also* U.S. Department of Justice, *Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act* 56-57 (2008) ("Indeed, the consensus at the hearings, and the predominant (but by no means unanimous) view among commentators, is that, in certain circumstances, predatory pricing can be a rational strategy for a firm with monopoly power facing a smaller competitor.").

2. Petitioners have suggested that *Trinko* mandates dismissal of a price-margin squeeze claim based on their assertion that any conceivable threat to competition posed by such a squeeze could be remedied by regulatory oversight. Petitioners' Brief at 35-37. They have relied on a section in *Trinko* discussing regulatory oversight that has no application to claims, such as a *Brooke Group* predatory pricing claim, that already fall within "'established antitrust standards.'" *Id.* at 406, 410-12. *Trinko*, having determined that the plaintiffs' "insufficient assistance" claims would not make a "recognized antitrust claim under this Court's existing refusal-to-deal precedents," looked to whether "traditional antitrust principles justify adding the present case to the few existing exceptions from the proposition that there is no duty to aid competitors." 540 U.S. at 410-11. In doing so, it stated that "[o]ne factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm." *Id.* at 412. Hence, the Court did not say that the existence of a regulatory scheme would serve to bar judicial enforcement of the antitrust laws, surely not for predatory pricing claims satisfying "'established antitrust standards.'" *Id.* at 406.

Further, with reference to the "implied immunity" doctrine discussed in *Trinko*, it is recognized that "[a]n implied immunity may be found only where there is 'a convincing showing of clear repugnancy between the antitrust laws and the regulatory system.'" *Phonetele, Inc. v. American Telephone & Telegraph Co.*, 664 F.2d 716, 726 (9th Cir. 1981) (Kennedy, J.) (citation omitted). And even then, an exemption will be implied "'only to the minimum extent necessary'" in order "'to make the

regulatory Act work.'" *Id.* at 730 n.37 (citation omitted). Further, "the mere existence of a [regulatory] remedy within the Act does not indicate a congressional intent to displace the antitrust laws." *Id.* at 735. This is true even though the remedial scheme under the Act involved "different substantive standards." *Id.* at 734 n.46. It is well established that the "freedom of a party injured by anticompetitive conduct to elect between an administrative [Federal Communications Act] remedy and a judicial cause of action under the Clayton Act is quite acceptable; the latter need not derogate or interfere with the former." *Id.*

Moreover, as the panel majority below recognized "the existence of regulation does not always eliminate the danger of anticompetitive harm." Pet. App. 15a. "The key, under *Trinko*, is the nature of the regulatory structure at issue." *Id.*; *see Trinko*, 540 U.S. at 412. Significantly, here, unlike *Trinko* and *Town of Concord*, the challenged conduct does not arise in the context of a fully regulated industry. Rather, as the Ninth Circuit panel majority recognized, there has been "no comparable regulatory attention paid to the retail DSL market" and hence any "restrictions on pricing at the retail level derive primarily from the antitrust laws." Pet. App. 18a; *see also Town of Concord*, 915 F.2d at 29 (recognizing the "special problem" posed by a price squeezing "monopolist, regulated at only one level, who seeks to dominate a second, unregulated level").

Petitioners refer to the FCC's decision not to subject Internet service to the "common-carrier regulation" duties imposed on ILECs for their provision of transmission facilities used to provide DSL service.

See National Cable & Telecommunications Ass'n v. Brand X Internet Services, 545 U.S. 967, 976, 993-94, 1001 (2005). Yet nothing in that determination suggests, much less establishes, that a "regulatory structure" exists "to deter and remedy anticompetitive harm" (*Trinko*, 540 U.S. at 412) of predatory retail pricing. Nor does it discredit the Ninth Circuit's panel majority view, apparently shared by Judge Gould (Pet. App. 22a), that restrictions on pricing at the retail DSL level derive primarily from the antitrust laws (*id.* at 18a). Nor does it demonstrate any tension, much less clear repugnancy, between the regulatory regime and the antitrust laws.

3. Recognition of a predatory pricing claim would not impermissibly impose administratively unwieldy "day-to-day" supervisory duties on antitrust courts, as was the case in *Trinko* with respect to alleged anticompetitive violations of the regulatory sharing requirements of the Telecommunications Act of 1996. *Trinko*, 540 U.S. at 415. Unlike "[e]ffective remediation of violations of regulatory sharing requirements [that] will ordinarily require continuing supervision of a highly detailed decree," redressing predatory retail pricing does not involve such "continuing supervision," any more than would be entailed in addressing any other below-cost predatory pricing schemes. *Id.* at 414-15. Courts have provided necessary and effective stewardship of the antitrust function in addressing predatory pricing.

Indeed, courts are needed and suited to redress such predatory retail pricing where as here "restrictions on pricing at the retail level derive primarily from the antitrust laws." Pet. App. 18a (panel majority decision).

That is particularly true in cases where the unregulated retail prices are set below the monopolists' own costs for providing service in order to exclude, or dominate, retail competition – and thereby raise prices and harm consumers. *See Town of Concord*, 915 F.2d at 28-29. In such cases, a court's "practicable ability" in assessing predatory pricing claims is no more difficult, and imposes no more "continuing supervision," than applying pricing and costs standards for any other predatory pricing claims under *Brooke Group*.

4. In the First Circuit's decision in *Town of Concord*, Justice (then Chief Judge) Breyer stated a pricing squeeze "does not ordinarily violate Sherman Act § 2 where the defendant's prices are regulated at both the primary and secondary levels." 915 F.2d at 22. As that court then clarified: "In so holding, we *are not* saying either that the antitrust laws do not apply in this regulatory context, or that they somehow apply less stringently here than elsewhere." *Id.* (emphasis in original). "And we have stressed that our reasoning applies with full force only when the monopolist who engages in the squeeze is regulated at both industry levels." *Id.* at 29.

The *Town of Concord* court further stated: "We recognize that a special problem is posed by a [price-squeezing] monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." *Id.* Such a "special problem" of anticompetitive harm as identified in *Town of Concord* would warrant antitrust court enforcement where regulated upstream monopolists engage in

predatory pricing conduct eliminating competition in an unregulated retail market, depriving consumers of lower prices, a choice of service providers, greater efficiency and enhanced products, as alleged here. J.A. 19-20 (¶ 24).

5. In sum, recognition of the validity of a predatory pricing claim would not promote competitors at the expense of lawful price competition, economic efficiency, or consumer welfare. Rather it is grounded in sound and settled antitrust principles directed at redressing predatory pricing conduct enabling the possession and exercise of monopoly power to the detriment of competition-consumer welfare that the antitrust laws were enacted to protect.

II. WHETHER RESPONDENTS HAVE STATED A VALID *BROOKE GROUP* CLAIM THAT WOULD SURVIVE UNDER THE *TWOMBLY* STANDARD, OR CAN STATE SUCH A CLAIM, NEED NOT AND SHOULD NOT BE DECIDED

Petitioners and the Government do not seem to dispute that the claims in respondents' amended complaint are "substantially similar" to those that survived *Brooke Group-Trinko* pleading attack in the Eleventh Circuit's *BellSouth* decision, as noted in the district court's 2005 Order ruling that "even if the *Brooke Group* requirements were applied, the [amended complaint] would satisfy those requirements." Pet. App. 48a-49a & n.16. Petitioners and the Government disagree with that ruling, while questioning whether the amended complaint and 2005 Order are even properly at issue here (*see* U.S. Merits Brief at 17;

Petitioners' Brief at 9 n.6). They correctly point out that this ruling, like the holding in *BellSouth*, was decided under the "no set of facts" standard (*Conley*, 355 U.S. at 45-46) subsequently repudiated by *Twombly*, 127 S. Ct. at 1969. But whether respondents do or can state a retail predatory pricing claim that would survive a pleading attack under the *Twombly* standard was not raised or decided below, and is best handled on remand, allowing respondents an opportunity to amend the complaint (as Judge Gould's dissent recommends) and having any amended pleadings then addressed under the *Twombly* standard.

A. Respondents' Price Squeeze Allegations of the Amended Complaint Were Substantially Similar to Those That *BellSouth* Held Stated *Brooke Group* Elements of Predatory Pricing

Respondents' price squeeze allegations in their amended complaint, which the district court ruled (in its 2005 Order) satisfied *Brooke Group* requirements, would have survived under the Eleventh Circuit's decision in *BellSouth* and the D.C. Circuit's own interpretation of its opinion in *Bell Atlantic*, reconciling that decision with the Eleventh Circuit's *BellSouth* decision allowing price squeeze claims to proceed on the basis of allegations like those here.

In addressing the sufficiency of the pleadings on the below-cost pricing requirement of *Brooke Group*, the court in *BellSouth* focused on allegations, like those of the amended complaint here, that retail prices for combined DSL and Internet access service were set below the prices charged at wholesale for the DSL

component alone. 374 F.3d at 1051. The court stated, "[i]f it is true that . . . the retail prices it is charging individual customers for combined DSL and Internet service, are 'below an appropriate measure of [BellSouth's] costs,' that fact suffices to satisfy the first prong of a price predation offense under § 2 of the Sherman Act." *Id.* at 1051-52 (citation omitted; brackets in original). The court added, "whether the unbundled wholesale loop prices BellSouth charges Covad pursuant to the interconnection agreement are the 'appropriate measure of [BellSouth's] costs' is a matter for the trier of fact to determine." *Id.* at 1052 (citation omitted; brackets in original); *see Brooke Group*, 509 U.S. at 222 n.1 ("Because the parties in this case agree that the relevant measure of cost is average variable cost, however, we again decline to resolve the conflict among the lower courts over the appropriate measure of cost.").

The *BellSouth* court noted that, as is true for the wholesale DSL transport prices here, the wholesale loop prices were determined, under the relevant regulation (there the 1996 Federal Telecommunications Act "FTCA"), using the "same baseline standard – namely, 'cost' – . . . as does the *Brooke Group* antitrust test of price predation." 374 F.3d at 1052. The court did not regard Covad's use of a regulation-based "at-cost measure" as contrary to "*Trinko*'s discussion of the FTCA's regulatory priority over antitrust law enforcement." *Id.* at 1051. The court stated "[t]o say that Covad's price squeezing claim defines the 'appropriate measure of [BellSouth's] costs,' in terms of an obligation created by the FTCA is to say very little when the FTCA itself relies upon 'cost' as the appropriate measure by which to determine

interconnection and network element rates." *Id.* at 1052 (citation omitted). Therefore, the court "conclude[d] that Covad's price squeezing claim is based on traditional antitrust standards." *Id.* It added, "[o]ur responsibility under *Trinko* to harmonize the Sherman Act and the FTCA does not entail excluding facially valid antitrust claims at the pleadings stage." *Id.*

Here, similarly, respondents' amended complaint's price squeeze claim alleges that petitioners' retail prices for their bundled service of DSL access, Internet service and equipment (modem and installation) were set below prices charged to their retail affiliate and respondents for the DSL access component. J.A. 36 (¶ 25(A)(3)). Hence, there is a plausible basis to suggest petitioners could not have been covering their costs for their bundled service when offered at a price below the cost incurred by the retail affiliate for the DSL component. As in *BellSouth*, the district court regarded such pleading sufficient to satisfy the "below-cost pricing" requirement of *Brooke Group*. Pet. App. 50a-51a.[16]

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16. Petitioners criticize using its DSL transport price, saying they are free to charge rivals a high "monopoly" price for the wholesale input and ignore that price in setting retail prices. Petitioners' Brief at 32-33 nn. 20-21. That criticism, however, does not render the DSL transport price (incurred by its own retail affiliate) as an irrelevant frame of reference for assessing "an appropriate measure of cost," at least at the pleading stage, where, as in *BellSouth*, it was a cost-based price. And here the retail service bundled the DSL transport component along with other services and equipment (for which costs were also incurred) at prices below that cost-based price for the DSL transport component. Petitioners suggest they may

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On the element of recoupment, the *BellSouth* court relied upon allegations that BellSouth was artificially allocating costs such that it was "compensating for deliberately reduced profits on the retail end of its operations with correspondingly greater profits on the wholesale side, in order to stifle competition from firms such as Covad that are both wholesale customers and retail rivals." 374 F.3d at 1051.[17]

The district court here looked at substantially identical allegations in respondents' amended complaint (*see* Pet. App. 49a; J.A. 36 (¶ 25(A)(3)), but disagreed with the *BellSouth* ruling that such allegations would, standing alone, suffice to state recoupment under *Brooke Group* (Pet. App. 51a). The district court concluded,

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acquire additional sources of revenues to augment that retail price. But this injects factual issues as to whether the revenues from the bundled retail service cover the cost of providing it; it does not render the DSL transport cost-based price an irrelevant frame of reference, at the pleading stage.

17. The court referenced allegations that:

> 'If BellSouth had charged itself the same wholesale price for loops, BellSouth could not make a profit from its DSL service at current prices. . . . As the costs are presently allocated, BellSouth must necessarily realize a significantly higher profit margin on its wholesale sales (for which it faces no competition) than it does on the corresponding retail sales (for which Covad is attempting to compete). BellSouth intended this artificial cost allocation to harm Covad, and it did.'

BellSouth, 374 F.3d at 1051.

> [n]onetheless the [amended complaint] elsewhere alleges something akin to a dangerous probability of recoupment within the meaning of *Brooke Group* . . . [alleging] that, as a result of [petitioners'] anti-competitive conduct, 'competition in the provision of Internet services has been effectively eliminated in [petitioners'] California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products.'

Pet. App. 51a-52a; J.A. 38 (¶ 26(b)). Further the amended complaint alleged that petitioners' retail affiliate had taken in excess of 80% of the relevant DSL market. J.A. 33 (¶ 20).

B. Challenges to the Sufficiency of Respondents' Predatory Price Squeeze Allegations Under *Twombly*, and Whether Respondents Can State a *Brooke Group* Predatory Retail Pricing Claim, Need Not and Should Not Be Addressed Here But Rather on Remand

The panel majority apparently did not believe these district court's *Brooke Group* rulings in its 2005 Order were before it or that it could or needed to address them.[18] And in the end, the appeals panel majority

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18. Petitioners had argued to the court of appeals, "even if *Trinko* did not bar their price squeeze claim, the Court should not reach the *Brooke Group* issue because that issue is not properly before the Court." 05-56023, Docket No. 25, Appellant's Reply Brief at 18 (2/21/06).

decision affirmed the district court's denial of petitioners' "motion for judgment on the pleadings," which was the ruling in the 2004 Order addressing the initial complaint, not the 2005 Order on the amended complaint. Pet. App. 19a; *see also* U.S. Merits Brief at 8 n.5. The panel majority decision does not address the sufficiency of respondents' allegations under *Brooke Group*, or whether respondents' price squeeze claims would need to meet the pleading requirements for a predatory pricing claim under *Brooke Group*. Hence, as the Government has explained, "it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal." U.S. Invitation Brief at 20; U.S. Merits Brief at 17.

Judge Gould's dissent does not discuss the 2005 Order rulings on *Brooke Group*. In any event, Judge Gould concluded respondents could not state an antitrust violation for price squeeze without satisfying the predatory pricing requirements of *Brooke Group* with respect to petitioners' pricing in the retail DSL service market, finding the amended complaint allegations deficient in that regard. Pet. App. 22a-23a.[19]

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19. As set forth above, respondents' amended complaint's price squeeze claim alleged *Brooke Group* elements along the lines deemed sufficient in *BellSouth*. And, as the district court ruled, the amended complaint additionally alleged "something akin to a dangerous probability of recoupment" in that, as a result of petitioners' anticompetitive conduct, "'competition in the provision of Internet services has been effectively eliminated in [petitioners'] California service areas, and consumers have been deprived of lower prices, a choice of service providers, greater efficiency and enhanced products.'"

(Cont'd)

But he "[did] not think it would be correct to dismiss the complaint on the pleadings with prejudice" because "we have not heretofore held that there must be a showing of market power in the retail market, nor held that the standards of *Brooke Group* must be applied in assessing predation in the retail side of a 'price squeeze.'" *Id.* at 23a. Instead, "after dismissal, [respondents] should have been free to amend their complaint if they could assert in good faith the allegations that are requisite here, after *Trinko*." *Id.* 23a-24a.

(Cont'd)

Pet. App. 51a-52a; J.A. 37-38 (¶ 26(b)). The amended complaint also alleged: (a) the market for DSL Internet service in petitioners' service region in California is a relevant market (J.A. 13 (¶ 11)); (b) petitioners have monopoly control over essential inputs to providing DSL service which cannot be practicably or reasonably duplicated (J.A. 28-29 (¶ 12), 31-32 (¶¶ 19-20)); and (c) petitioners' retail affiliate has in excess of 80% of the relevant DSL market (J.A. 33 (¶ 20)). Respondents believe the allegations of their amended complaint, albeit framed as a "price squeeze" claim, satisfy the elements of a retail predatory pricing-monopolization claim. But, in any event, as Judge Gould's dissent recommends, respondents should be allowed the opportunity to plead allegations of a pure (standalone) predatory retail pricing claim as outlined in his dissent. Pet. App. 22a ("'price squeeze' . . . boils down to a claim of a predatory pricing on sales of internet connections by [petitioners] in the retail market"); *id.* at 24a n.2 ("the district court . . . should have permitted amendment in case the critical allegations [of a *Brooke Group* predatory retail pricing claim] can be made by the [respondents]" as "[t]here is just enough possibility of an injury occurring for reasons culpable under the antitrust laws, *see Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477 (1977)").

Agreeing with Judge Gould, petitioners and the Government argue that the amended complaint price squeeze allegations are insufficient to satisfy *Brooke Group* and the district court's ruling to the contrary was decided under the "no set of facts" pleading standard repudiated in *Twombly*. Nonetheless, under Judge Gould's recommended disposition, petitioners, on remand, will have the opportunity to challenge whether any amended complaint satisfies the requirements of a *Brooke Group* predatory pricing claim under the *Twombly* pleading standard. Respondents believe that is the proper course to proceed, particularly since it is "unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal" (U.S. Merits Brief at 17), and the *Twombly* issue was not raised or decided below.[20]

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20. As the Government has stated, "[t]o be sure, the Court might lack jurisdiction to decide the distinct question[] . . . whether the amended complaint alleged a [*Brooke Group* predatory pricing] claim, but [that] question[] would not merit this Court's review at this time in any event." U.S. Invitation Brief at 20 n.8.

CONCLUSION

The judgment should be, as suggested by Judge Gould's dissent, vacated and the case remanded for further proceedings in the district court consistent with the substantive law as set forth in Judge Gould's dissent.

Respectfully submitted,

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REPLY BRIEF

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IN THE
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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November 13, 2008

CORPORATE DISCLOSURE STATEMENTS

Petitioners' Rule 29.6 Statements were set forth at page iii of their opening brief, and there are no amendments to those Statements.

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INTRODUCTION

The Ninth Circuit held that respondents had stated a claim under Section 2 of the Sherman Act by alleging that AT&T engaged in a price squeeze – even though AT&T had no antitrust duty to deal with respondents at all. That holding conflicts with *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), and this Court's Section 2 jurisprudence, and the Court should reverse the judgment of the court of appeals.

After defending the Ninth Circuit's price-squeeze holding at the petition stage, respondents now confess that the Ninth Circuit erred and that their price-squeeze claim survives *Trinko only* if respondents allege that AT&T engaged in predatory retail pricing. *See* Resp. Br. 13, 18, 41. Respondents' concession, while not "dispositive of [the] legal issue," provides "further indication" that the opinion below is erroneous. *Roberts v. Galen of Virginia, Inc.*, 525 U.S. 249, 253 (1999) (per curiam).

Amici's suggestion that respondents' concession renders the case either moot or inappropriate for review on the merits is incorrect. Respondents have not abandoned their Section 2 claim, nor have they even conceded that the district court's failure to grant AT&T's motion for judgment on the pleadings was erroneous. The parties thus remain adverse, and this Court has jurisdiction. Moreover, all of the reasons that counseled in favor of review in the first place – including the chilling effect of the Ninth Circuit's decision on pro-competitive conduct – still counsel in favor of resolution of the question presented.

Amici's defense of "price squeeze" as an "independent antitrust tort," Comptel Br. 2, fails to provide any justification for imposition of the competitor-protecting duty that the doctrine embodies. *First*, their arguments fail to reckon with *Trinko*, which teaches that, in the absence of a duty to deal under the antitrust laws, complaints about the terms under which a monopolist deals – even if such dealing is compelled by regulation – fail to state a claim under Section 2. *Second*, and more fundamentally, *amici* offer no persuasive reason to believe that any harm from price squeeze – as distinct from unlawful refusal to deal or predatory pricing – is significant, practically identifiable, or subject to court-ordered remedy; by contrast, the consumer harm from recognition of price squeeze as a basis for liability is both substantial and pervasive. Price-squeeze doctrine forces vertically integrated producers to pull their competitive punches with respect to efficient production and aggressive pricing, and it deters voluntary dealing. The Court should accordingly reject allegations of price squeeze as a basis for potential liability under Section 2.

ARGUMENT

I. RESPONDENTS' CONCESSION THAT THE NINTH CIRCUIT ERRED SUPPORTS REVERSAL BUT DOES NOT AFFECT THE NEED FOR REVIEW ON THE MERITS

A. The Ninth Circuit Should Have Reversed the District Court's Denial of AT&T's Motion for Judgment on the Pleadings

1. AT&T maintains that the district court erred in failing to grant AT&T's motion to dismiss respondents' complaint. The Ninth Circuit disagreed and affirmed the district court's decision "because [respondents'] allegation that [AT&T's] pricing scheme created an anticompetitive price squeeze states a potentially valid claim under § 2 of the Sherman Act." Pet. App. 19a.

In opposing the petition for certiorari, respondents defended the Ninth Circuit's holding and its reasoning, contending that allegations that a vertically integrated monopoly "intentionally charged . . . wholesale prices that were too high in relation to" retail prices state a claim, despite this Court's ruling in *Trinko*. Br. in Opp. 1; *see also id.* at 3 (asserting that "price squeeze claims need not satisfy the predatory pricing requirements of" *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993)), 16-17 & n.8.

Without explaining – or even acknowledging – their change of position, respondents now concede that the legal rationale underlying the decision of the panel majority is in error, stating that "it is clear respondents' pricing [sic] squeeze claim survives *Trinko* only if it satisfies the requirements of a predatory retail pricing claim under *Brooke Group*." Resp. Br. 13. Respondents accordingly urge the Court

to vacate the decision of the Ninth Circuit and to remand the case "with instructions that respondents be given leave to amend their complaint to allege, if they can, a valid retail predatory pricing claim under *Brooke Group*." *Id.* at 18.

The Court *should* vacate the decision below, making clear that the answer to the question presented is "no." A plaintiff does *not* state a claim under Section 2 by alleging that a vertically integrated monopolist with no antitrust duty to deal has left an insufficient margin between wholesale and retail prices to allow wholesale customers to compete at the retail level. *Cf.* Pet. i. Respondents' failure to contest the point in its merits brief, while not controlling, is, as this Court has recognized in the past, a strong indication that the position respondents defended at the certiorari stage is indefensible. *See Galen of Virginia*, 525 U.S. at 253.

2. The Court should also hold that the complaint failed to state a claim under Section 2 and should have been dismissed. The possibility to which respondents devote the bulk of their merits brief – that respondents could have stated a claim by alleging retail-level predatory pricing – cannot save the complaint. Respondents, represented by sophisticated antitrust counsel, deliberately chose not to allege predatory pricing. This Court's *Brooke Group* decision clearly sets out the elements of a predatory-pricing claim: creation or maintenance of monopoly power through the setting of prices below cost, combined with a likelihood of recoupment of losses associated with below-cost pricing. *See* 509 U.S. at 223. Yet, as the dissent below recognized, the complaint does not "allege that the seller had the market power to set prices for internet connection[s] in the

retail market, that [AT&T's] retail price . . . was set below cost, [or] that losses could later be recouped." Pet. App. 23a. The dissent was discussing the allegations of the substantively identical *amended* complaint, but the same observations apply at least as strongly to the original complaint.[1] Accordingly, the Court should remand with instructions to dismiss the complaint. Whether further amendment should be permitted is a matter the district court can address in the first instance.

B. Respondents' Concession Does Not Deprive the Court of Jurisdiction or Lessen the Importance of the Question Presented

Amici, but not respondents, argue that respondents' concession that the Ninth Circuit erred somehow moots the case. *See* AAI Br. 4; Comptel Br. 6-7. The argument is incorrect: this Court's jurisdiction is intact, and there is no prudential reason to refrain from deciding the question presented. To the contrary, all the considerations that warranted review in the first place still counsel in favor of deciding the case on the merits.

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[1] Respondents argue that they have alleged below-cost pricing because the price AT&T charged for retail Internet-access service was, for a "period," below the price AT&T charged for DSL Transport. *See* Resp. Br. 35 & n.16. But there is no allegation (and no regulatory requirement) that DSL Transport prices be set at cost, and no justification for accepting respondents' quite different allegations regarding relative wholesale and retail prices as an allegation that retail prices were below AT&T's own costs. *See also* 2 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 307, at 95 (3d ed. 2008) ("[I]f pricing is alleged to be predatory, then the plaintiff must plead prices below cost, because the Supreme Court has established that requirement as a matter of law.").

1. Comptel asserts in passing (at 2) that "Article III of the Constitution" requires the Court to dismiss the petition. But the fact that respondents intend to pursue their Section 2 claim is sufficient to establish that the parties are adverse for Article III purposes. For example, in *Cardinal Chemical Co. v. Morton International, Inc.*, 508 U.S. 83 (1993), both the petitioner and the respondent agreed that the only aspect of the Federal Circuit's decision under review – that is, the court's decision to vacate a finding of patent invalidity as moot – was wrongly decided. But the Court rejected the possibility that the parties "lack[ed] the adversarial posture required by Article III." *Id.* at 88 n.9. Rather, while the parties "d[id] agree on the correct answer to the question presented," they remained adverse with respect to their ongoing dispute. *Id.* The same is true here. *See also id.* at 104 (Scalia, J., concurring in relevant part) (even "the parties' total agreement as to disposition of this case poses no constitutional barrier to its resolution").[2]

This Court not infrequently decides cases where the respondent declines to defend the judgment of the court of appeals. For example, in *Forney v. Apfel*, 524 U.S. 266 (1998), the United States agreed with the petitioner that the Ninth Circuit erred in dismissing the petitioner's appeal; the Court appointed an *amicus* to defend the court of appeals' decision and reversed. *See id.* at 269. In *Mackey v. Lanier Collection Agency & Service, Inc.*, 486 U.S. 825

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[2] The parties do not in fact agree on the proper disposition of this case: petitioners seek an order directing the dismissal of respondents' Section 2 complaint, while respondents ask for a remand with leave to amend their Section 2 claim. *Compare* Pet. Br. 37 *with* Resp. Br. 33 ("whether respondents do or can state a retail predatory pricing claim . . . is best handled on remand").

(1988), the respondent "elected not to appear"; rather than dismiss the case, the Court appointed an *amicus* to defend the judgment so that it could reach the merits. *Id.* at 829 n.3. Disagreement between the parties over the legal issue presented was also lacking in *Toibb v. Radloff*, 501 U.S. 157, 160 n.4 (1991); *INS v. Chadha*, 462 U.S. 919, 931 (1983); aspects of *Bob Jones University v. United States*, 461 U.S. 574, 585 n.9 (1983); and *Granville-Smith v. Granville-Smith*, 349 U.S. 1, 4 (1955), to name a few.[3]

Amici cite *Deakins v. Monaghan*, 484 U.S. 193 (1988), but in that case the respondents did not "confess error" on the question presented. Rather, the respondents stated that they would no longer seek the equitable relief in federal court that was the subject of the court of appeals' disputed ruling. *See id.* at 198-99. Making clear that the respondents' representation – and the Court's reliance on it – would mandate "dismissal with prejudice" of those injunctive claims, the Court concluded that the question of the federal courts' authority to render that relief was moot. *Id.* at 200; *see also Webster v. Reproductive Health Servs.*, 492 U.S. 490, 512-13 (1989) (noting that appellees' decision "to no longer seek a declaratory judgment that [a statutory provision] is unconstitutional" meant that challenge to provision was moot). Here, by contrast, respondents have made clear that they intend to continue to pursue their Section 2 claim against AT&T.

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[3] Likewise, in the criminal context, while "[c]onfessions of error are . . . entitled to and given great weight, . . . they do not relieve this Court of the performance of the judicial function." *Sibron v. New York*, 392 U.S. 40, 58 (1968) (internal quotation marks omitted).

2. *Amici*'s suggestion that the Court should decline to reach the merits on prudential grounds, *see* Comptel Br. 2, 6-7, is likewise incorrect. AT&T's petition emphasized that the Ninth Circuit's embrace of price-squeeze doctrine would, if left unreviewed, "deter conduct that enhances efficiency." Pet. 23. The United States agreed, noting that "review is warranted because the Ninth Circuit's endorsement of [price-squeeze] theory threatens to chill retail price-cutting . . . and encourage litigation designed to protect competitors at the expense of competition, thereby undermining the procompetitive purposes of the antitrust laws and harming consumers." U.S. Cert. Br. 7. *Amici* cite as good law decisions from the Second, Third, and Seventh Circuits that endorse price squeeze as an independent basis for antitrust liability. *See* Comptel Br. 8-10. And the risk of consumer-harming consequences is accentuated by the public statement of the Federal Trade Commission supporting the Ninth Circuit's decision and endorsing the price-squeeze theory of liability. *See* Pet. Br. 21.

The Court's grant of certiorari reflects the importance of the question presented. *See* Sup. Ct. R. 10. The antitrust policy concerns that warranted review in the first place transcend the case-specific consequences of the Ninth Circuit's ruling and continue to argue compellingly in favor of a decision by this Court on the merits. *See Friends of the Earth, Inc. v. Laidlaw Envtl. Servs. (TOC), Inc.*, 528 U.S. 167, 191-92 (2000) ("To abandon the case at an advanced stage may prove more wasteful than frugal."). Two *amicus* briefs defending the Ninth Circuit's decision on the

merits ensure that the Court will have the benefit of full adversarial presentation of the issues.[4]

II. THE NINTH CIRCUIT'S RULING CONFLICTS WITH THIS COURT'S ANTITRUST JURISPRUDENCE

A. *Trinko* Bars Respondents' Claim

Respondents' price-squeeze claim depends on the allegation that the combination of AT&T's wholesale and retail prices placed respondents "at a serious unfair disadvantage vis-a-vis" AT&T in the sale of DSL-based Internet-access service. Compl. ¶ 19 (JA17). But that is precisely the duty that *Trinko* rejects: "alleged insufficient assistance in the provision of service to rivals" fails to state a claim in the absence of any antitrust duty to deal at all. 540 U.S. at 410; *see* Pet. Br. 17-21; U.S. Br. 11-15; Verizon/NAM Br. 5 ("The focus on prices specifically does not take linkLine's claim outside the scope of *Trinko*'s rejection of a duty to deal.").

Amici's efforts to distinguish respondents' price-squeeze claim from the allegations at issue in *Trinko* come to nothing. Comptel asserts (at 28) that *Trinko* "did not address the viability of a price squeeze claim," but it can offer no reason that the price squeeze alleged here presents any antitrust concern that would justify treating it as distinct from the allega-

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[4] If the Court were to decline to address the merits of the question presented, it would also invite gamesmanship by respondents that have a repeat-player interest in preserving a ruling of dubious validity. *Cf. U.S. Bancorp Mortgage Co. v. Bonner Mall P'ship*, 513 U.S. 18, 25 (1994). In this regard, it is worth noting that respondents nowhere even *commit* to abandon their price-squeeze claim; while they concede the error of the Ninth Circuit's holding, they do not promise that they would not take advantage of that error if given the opportunity.

tions of inadequate assistance at issue in *Trinko*.[5] In fact, there is *no* reason, because the asserted antitrust impact – restriction on the effectiveness of downstream competitors – is the same. *See* Pet. Br. 20-21.

AAI seeks to recast *Trinko* as reflecting exclusively "institutional concerns," AAI Br. 29, and it argues that such concerns are attenuated in the case of certain price squeezes, *see id.* at 30-37. The assertion that price-squeeze claims are easier for a court to evaluate and remedy than the specific allegations in *Trinko* is incorrect. *See* 3B Areeda & Hovenkamp ¶ 787d, at 376 ("As Judge Breyer explained in [*Town of Concord v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990)], price 'squeeze' claims are probably as difficult to administer as refusal to deal claims, thus suggesting that such claims should fare no better under *Trinko* than the essential facility claim involved in that case."); *see also* Pet. Br. 30-33; *infra* pp. 18-20. More fundamentally, the Court's rejection of a duty to deal in *Trinko* was based not merely on the concern that imposition of sharing duties imposes inappropriate regulatory responsibilities on courts; rather, it reflected first of all the recognition that forced sharing undermines incentives to invest and

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[5] Comptel argues (at 29-30) that *Trinko* involved conduct in the upstream market but a price-squeeze claim also involves conduct in the downstream market – that is, the setting of retail prices too low relative to what rivals may find comfortable. That argument ignores the fact that in *Trinko*, too, the upstream conduct was subject to challenge only because it allegedly rendered retail rivals' services *relatively* unattractive in comparison to the defendant's. *See* Pet. Br. 20; Verizon/NAM Br. 5 ("[T]he duty to deal asserted, and rejected [in *Trinko*], was a duty to deal on terms that would enable at least some rivals to compete in the retail market.").

to innovate and threatens to restrict, not to promote, meaningful competition. *See* 540 U.S. at 407-08. All of these concerns apply equally to the particular allegations of price squeeze at issue here.

B. Recognition of Price-Squeeze Claims As an Independent Antitrust Tort Is Contrary to Precedent and Sound Antitrust Policy

Amici argue that recognition of price-squeeze claims – over and above predatory-pricing and refusal-to-deal doctrines – can forestall consumer harm with limited risk of deterring conduct that benefits consumers. That argument is wrong at the threshold in suggesting that a price squeeze even theoretically implies cognizable consumer harm. And, in any event, *amici* do not remotely justify the assertion that any benefits from establishing price-squeeze claims as available Section 2 grounds could reliably outweigh the plain, severe risks of harm from doing so. *Amici* simply ignore the competition-deadening impact of a rule that requires a wholesale monopolist to protect downstream rivals and understate the institutional objections to price-squeeze doctrine. Finally, in arguing that the regulatory context provides a reason to recognize respondents' price-squeeze claim, *amici* have matters backwards. The existence of regulation argues against recognition of a quasi-regulatory price-squeeze-avoidance duty under the antitrust laws.

In cases where it is argued that a price squeeze constitutes a constructive refusal to deal, such a claim can and should be dealt with under the law of refusal to deal. *See* U.S. Br. 14 n.8. Likewise, in cases where it is argued that a price squeeze constitutes predatory pricing, such a claim can and should be dealt with under *Brooke Group*. The

"price squeeze" rubric adds nothing but mischief and confusion to these two doctrines, which are carefully designed to protect competition and consumers, not competitors. Despite the extensive secondary literature that AAI cites, not a single commentator advocates imposition of liability for margin-based price squeeze under Section 2.

1. The existence of a price squeeze does not support any inference of consumer harm

Both AAI and Comptel argue that elimination of downstream competitors through a price squeeze may restrict consumer choice, hamper innovation, and raise barriers to entry in the upstream market. *See* AAI Br. 12-15; Comptel Br. 14-15. The invocation of such potential consequences provides no justification for condemnation of price squeezes because (1) the elimination of competitors is not *itself* sufficient basis to infer harm to competition – any form of vigorous pro-competitive conduct harms competitors but benefits consumers – and (2) in any event, *amici* identify no incremental harm from price squeeze as distinct from an outright refusal to deal.

a. *First*, the fact that unilateral conduct disadvantages or even eliminates rivals does not establish that *competition* has been harmed in the relevant sense. *See* Pet. Br. 22-26; U.S. Br. 19-21; Verizon/NAM Br. 18-20. Harm to rivals is inherent in competition: "almost all business activity, desirable and undesirable alike, seeks to advance a firm's fortunes at the expense of its competitors." *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 21 (1st Cir. 1990) (Breyer, J.). But actions that harm rivals may nevertheless benefit consumers by promoting investment and economic efficiency. This Court's anti-

trust jurisprudence is built on this basic distinction between "protection of *competition*" and protection of "*competitors*." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (internal quotation marks omitted).

AAI argues that a price squeeze should be subject to scrutiny if "the monopolist could not have made a profit by selling at its retail rates if it had purchased at its own wholesale rates," what it refers to as a "transfer price test." AAI Br. 10. But the "transfer price test" proposed by AAI is inconsistent with two important principles governing unilateral pricing decisions. As this Court held in *Trinko*, a legitimate monopolist's "opportunity to charge monopoly prices" is "an important element of the free-market system." 540 U.S. at 407. At the same time, there is no restriction on charging low downstream prices, so long as those prices are above cost. *See Brooke Group*, 509 U.S. at 223; *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990).

AAI's standard would force a monopolist either to increase retail prices, to abandon (or avoid) partial vertical integration (either by avoiding voluntary dealing or by exiting the downstream market), or to forgo the charging of monopoly prices. *See* 3B Areeda & Hovenkamp ¶ 767d2, at 145-46. To the extent a monopolist will generally avoid surrendering monopoly profits, it will follow one of the first two courses and consumers will be harmed. *See id.* at 146. Furthermore, such a rule discourages investment where it may matter most – upstream – because enforcement of a price-squeeze-avoidance duty guarantees the downstream rival a share in any improvements at the wholesale level. *See Trinko*, 540 U.S. at 407-08. "[I]t hardly seems to make antitrust sense

to say to a vertically integrated monopolist that it must not only take in non-integrated competitors but take tender care of them as well." 3B Areeda & Hovenkamp ¶ 767d2, at 146.

We explain below that a rule that subjects price squeezes to antitrust scrutiny deters pro-competitive conduct because of the risk of false condemnations and the costs associated with litigation of even unsuccessful claims. *See infra* pp. 17-18; Verizon/NAM Br. 9-17. But, even if the "transfer price test" could be perfectly and costlessly administered, there would still be no basis for concluding that it would prevent harm to competition rather than competitors. Indeed, "it is difficult to see any *competitive* significance [to a price squeeze] apart from the consequences of vertical integration itself." 3B Areeda & Hovenkamp ¶ 767c, at 137.[6] The argument that a price squeeze can eliminate competitors; that the elimination of downstream competitors may raise barriers to entry or impair non-price competition; and that therefore price squeezes should be subject to scrutiny under Section 2 simply proves too much.

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[6] "[A]lthough it is possible to produce situations where a price squeeze leads to competitive harm, even in these cases it is possible that the results could go the other way and there would be no competitive harm." Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct?*, 4 J. Competition L. & Econ. 271, 276 (2008). As Judge Easterbrook has explained, the point is not that challenged unilateral conduct "'never' could injure consumers"; rather, it is that there is no reason to conclude that the existence of a price squeeze causes consumer harm in circumstances that are both common enough and sufficiently easy to describe and identify to justify the costs of subjecting the conduct to scrutiny. *Schor v. Abbott Labs.*, 457 F.3d 608, 612-13 (7th Cir. 2006), *cert. denied*, 127 S. Ct. 1257 (2007); *see infra* pp. 17-18.

Comptel argues (at 11-13) that price squeezes create the same type of harm as predatory pricing but with "far greater possibility of financial reward" and "substantially less" risk of false positives. The argument is misguided on every point. First, predatory pricing is of concern under the antitrust laws because it has the potential to eliminate *independent* competitors that would otherwise constrain the monopolist's ability to charge monopoly prices. By contrast, the antitrust laws do not prevent a monopolist from continuing to charge a monopoly price at the upstream level, and there is no reason to suppose that the presence of a downstream competitor will, as a general matter, constrain downstream pricing.

Second, the potential reward from predatory pricing is the creation of a monopoly that did not exist before (or preservation of a monopoly that is otherwise threatened), rewarding the successful predator with otherwise unavailable monopoly profits. By contrast, a wholesale monopolist already earns monopoly profits and, in general, benefits from the *presence* of efficient downstream rivals, not from their absence. *See* Pet. Br. 24.[7]

Third, the law of predatory pricing limits the risk of false positives by establishing a simple rule that above-cost pricing is lawful *per se*. By contrast, a rule that bases potential liability on the existence of

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[7] That there may be exceptions to the rule that a monopolist cannot earn additional monopoly profits by gaining monopoly power in a vertical market, *see* AAI Br. 16, hardly alters the analysis: exceptions to the rule are themselves difficult to identify in practice and essentially impossible to embody in a workable rule of law. *See Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (1st Cir. 1983) (Breyer, J.). In any event, here, the downstream service and upstream input are in a one-to-one ratio. *See* Pet. Br. 24.

a price squeeze (including, in Comptel's view (at 18-19), a squeeze that results from retail pricing that equals the sum of "wholesale . . . price *and* the costs of the additional inputs included in the retail product") not only places upward pressure on retail prices, but also discourages efficient voluntary dealing and vertical integration.

b. *Second*, *amici* offer no reason to conclude that a price squeeze causes any harm to competition that is distinct from an outright refusal to deal with the downstream competitor. Yet that is the relevant harm. Indeed, a "first cut in the antitrust analysis" in *any* case should be "to query whether the defendant has any duty to deal with the plaintiff at all." 3B Areeda & Hovenkamp ¶ 767c, at 138. If there is not, "it makes no sense to prohibit a 'predatory' price squeeze." *Id.* ¶ 767c5, at 142.

This conclusion is not *merely* a case of the "greater includes the lesser," *see* AAI Br. 27-28; Comptel Br. 30, though it should be enough "[i]n general and in the present setting" to rely on that principle, *In re Catt*, 368 F.3d 789, 792 (7th Cir. 2004) (Posner, J.).[8] Rather, any incremental benefit to competition from restricting the terms of dealing that is not compelled under the antitrust laws is overwhelmed by the

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[8] *Amici* provide no example in the Section 2 context where the principle does not hold. AAI claims that a manufacturer may "refuse to deal with a retailer that fails to adhere to the manufacturer's suggested retail prices" but may not necessarily "suspend[] the retailer for a short period." AAI Br. 27-28 (citing *United States v. Parke, Davis & Co.*, 362 U.S. 29, 44 (1960)). But *Parke, Davis* involved the distinction between a *per se* lawful unilateral refusal to deal and *agreement* between a manufacturer and a distributor to charge a minimum resale price, which is subject to scrutiny under *Section 1*. It had nothing to do with prohibiting "less drastic" unilateral conduct. *Cf.* AAI Br. 27.

negative systemic effects of subjecting such price squeezes to scrutiny. In short, as the government explains, *amici*'s argument amounts to urging that AT&T must deal on price terms that would preserve respondents' profit margin, even though AT&T has no obligation under the antitrust laws to deal with respondents at all. *See* U.S. Br. 14. *Amici* have not remotely justified that illogical claim.

2. Recognition of price-squeeze claims would deter pro-competitive conduct

Amici do not dispute that a price squeeze may arise from conduct that benefits consumers – efficient vertical integration and retail price-cutting. And they cannot seriously question that a rule that penalizes such squeezes tends to increase prices, deter voluntary dealing, and discourage efficient downstream entry. Instead, they argue that these matters can be dealt with by "scrutiniz[ing] individual price squeeze claims, at later stages of litigation." Comptel Br. 15; *see* AAI Br. 20.

That argument should provide no reassurance, because any rule that makes the existence of a price squeeze a sufficient basis for antitrust scrutiny will pervasively discourage conduct that could give rise to a charge of price squeeze, even if justifications are permitted.[9] This is true in part because of the risk of

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[9] Just as misguided is AAI's suggestion that liability should turn on whether "the price squeeze was specifically intended to foreclose competition from unintegrated rivals." AAI Br. 22. Aside from the emptiness of the formulation – efficient vertical integration may be specifically intended to foreclose competition from unintegrated rivals and is nonetheless beneficial for that – this Court has made clear that the claim that conduct was motivated by hostility to competitors is immaterial to antitrust analysis. *See Brooke Group*, 509 U.S. at 225. Most vigorous

false positives, which "counsels against an undue expansion of § 2 liability." *Trinko*, 540 U.S. at 414. It is also true because even a successful defense of an antitrust claim – particularly if it comes at the end of a long discovery road – imposes substantial costs on a defendant. *See Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1967 (2007) (noting finding that "discovery accounts for as much as 90 percent of litigation costs when discovery is actively employed"); *see also id.* at 1967 n.6. Under the approach advocated by *amici*, a competitor is forced to weigh the risks of liability and the greater risk of litigation costs when evaluating the costs and benefits of vertical integration, voluntary dealing, or retail price cuts. That risk is exacerbated in this context by the reality that downstream rivals may have every incentive to wield the threat of litigation in order to induce a vertically integrated rival to "pull[] its competitive punches." *Olympia*, 797 F.2d at 375; *see* Pet. Br. 26 n.15; *id.* at 27 n.16 (noting risk of collusion). When such anticompetitive consequences are weighed against the questionable risk of incremental consumer harm from a price squeeze, it is particularly clear that subjecting such conduct to scrutiny is "not worth the candle." *Schor*, 457 F.3d at 613.

3. Price-squeeze doctrine forces courts to act as regulators

In part because they neither clearly articulate nor agree on a price-squeeze standard, *amici* offer no answer to the concern that enforcement and remedy of such a duty would impose inappropriate administrative burdens on courts. *See* Pet. Br. 30-33. Rather,

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competition shares that motivation. *See Olympia Equip. Leasing Co. v. Western Union Tel. Co.*, 797 F.2d 370, 379-80 (7th Cir. 1986) (Posner, J.).

they argue that administrative concerns may be attenuated when the defendant's wholesale prices exceed its own retail prices. *See* AAI Br. 30; Comptel Br. 17-18.

As an initial matter, there is no more reason to believe that a wholesale-exceeds-retail price squeeze will harm competition than that any other price squeeze will do so – such a pricing pattern may simply reflect market conditions, and, in any event, consumers benefit from the reduction in retail prices, even if competitors suffer losses. The objection that there can generally be no antitrust harm from such a squeeze distinct from the harm associated with an outright refusal to deal (presumptively lawful here) holds good.

More to the point, the wholesale-exceeds-retail benchmark does little to alleviate institutional concerns. As previously noted, the retail price need not reflect the full *revenue* benefits of retail sales. *See* Pet. Br. 32-33 & n.21. That is particularly true where a narrow focus on an individual retail service – here, DSL-based Internet-access service – fails to take account of the business importance of sales of packages of services to consumers. For example, a customer who purchases voice service and DSL-based broadband service from a single provider may be less likely to switch *both* voice and broadband service to a competing provider; as a result, the expected revenue benefit from retail broadband sales must take account of voice revenues as well. And all of this ignores the fact that the relationship between wholesale and retail prices is not static.[10] In sum, sorting out these

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[10] The original complaint here made no reference to wholesale prices exceeding retail prices at any point. And the amended complaint simply states that they did so for a "period

facts and evaluating their competitive significance would impose unmanageable tasks on the court and would invite costly errors.

4. Consideration of the regulatory context supports dismissal

Amici argue that recognition of a price-squeeze claim is appropriate here because (1) AT&T is subject to price regulation at the wholesale but not at the retail level, and (2) wholesale-price regulation may be ineffective. *See* AAI Br. 17-19, 31-34; Comptel Br. 19-26. But, far from providing a justification for recognizing an unprecedented price-squeeze-avoidance duty under the antitrust laws, the presence of regulation provides a further reason to reject respondents' claim. *See* Pet. Br. 35-37.

First, *amici* offer no coherent basis for believing that the regulatory context provides either means or motive for conduct that would raise any antitrust concern. Comptel argues simultaneously that AT&T is motivated to squeeze downstream competitors – so as to earn monopoly profits denied at the wholesale level, *see* Comptel Br. 19-21 – and that AT&T is not effectively regulated at the wholesale level at all, *see id.* at 24-26; *see also* AAI Br. 31-34. The assertions are mutually contradictory; more important, neither provides any basis for recognition of price-squeeze liability in general or in this case. To the extent AT&T is subject to strict pricing regulation at the wholesale level, the regulator has authority to take retail rates -- and downstream rivals' complaints about price squeeze – into account in setting those

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of substantial time," Am. Compl. ¶ 20 (JA33) – which is entirely consistent with the fact that wholesale prices were *generally* below retail prices.

rates. And, to the extent AT&T is *not* subject to effective price regulation at the wholesale level, avoidance of price regulation at the wholesale level would provide no incentive to engage in a price squeeze.

Amici ultimately argue that, in the absence of effective regulatory enforcement, a monopolist can use a price squeeze to "forc[e] out competition." Comptel Br. 26. But that argument does not distinguish the situation in which there is regulation from a price squeeze in an unregulated market, and the existence of regulation is therefore essentially irrelevant to the antitrust analysis. Indeed, *amici* may not rely on the existence of a *regulatory* duty to deal to justify enforcement, under the antitrust laws, of an obligation to avoid a price squeeze: *Trinko* demonstrates that "the antitrust laws should not be used to enforce what boils down to a regulatory obligation to deal." U.S. Br. 14, 28.

Second, *amici*'s argument that regulation is ineffective in this context rings hollow in light of respondents' failure ever to pursue a challenge to AT&T's rates before the responsible agency. There is no dispute that the Federal Communications Commission ("FCC") has the *authority* to address price-squeeze concerns under the just-and-reasonable standard, and it can do so based on expertise and with the flexibility to adapt to changing conditions. *See* Pet. Br. 35-36.[11] Given the existence of this regulatory structure, it would be particularly in-

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[11] For whatever it is worth, after the period covered by the complaint, the FCC imposed – as a condition of approval of AT&T's merger with BellSouth – a requirement that AT&T set the wholesale price for DSL Transport no higher than the retail price of AT&T's own DSL-based Internet-access service. *See* Pet. Br. 5 n.4.

appropriate to impose a price-squeeze-avoidance duty under the antitrust laws.

CONCLUSION

The judgment of the court of appeals should be reversed and the case remanded with instructions to dismiss the complaint.

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SUPPLEMENTAL BRIEF

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No. 07-512

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IN THE

Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY D/B/A AT&T CALIFORNIA, *et al.*,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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Respondents submit this supplemental brief to call attention to an intervening matter not available at the time of respondents' last filing. On May 22, 2008, the Solicitor General, in response to this Court's order inviting it to express the views of the United States, filed its "Brief for United States as Amicus Curiae" recommending granting the petition for writ of certiorari. On May 23, 2008, the Federal Trade Commission issued its "Statement of the Federal Trade Commission" concerning that amicus brief, stating that the Commission "declines to join the U.S. Department of Justice in recommending that the U.S. Supreme Court review the Ninth Circuit's decision in *linkLine Comm'n v. Pacific Bell Telephone Co.*, 503 F.3d 876 (9th Cir. 2007), because we disagree with DOJ's analysis, and because this case does not appear to be worthy of review at this time. The vote was 3 - 0 with Chairman Kovacic recused." (Respondents' Supplemental Brief Appendix at 4a.) "In the interests of transparency, [the Federal Trade Commission's] statement describes the reasons for the Commission's decision." (*Id.* at 4a-14a.) That statement can be found as a link to the Commission's press release of its issuance on the Commission's website at *http://www.ftc.*gov/opa/2008/05/linkline.shtm.

Respectfully submitted,

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APPENDIX

APPENDIX — STATEMENT OF THE FEDERAL TRADE COMMISSION REGARDING U.S. SOLICITOR GENERAL'S *AMICUS* BRIEF FILING IN *PACIFIC BELL TELEPHONE COMPANY v. LINKLINE COMMUNICATIONS*

Federal Trade Commission
Protecting America's Consumers

For Release: May 23, 2008

FTC Issues Statement Regarding Solicitor General's *Amicus* Brief Filing in *Pacific Bell Telephone Company v. linkLine Communications*

Today the Federal Trade Commission announced that it has decided not to join an *amicus* brief filed by the Department of Justice urging the Supreme Court to grant certiorari in *Pacific Bell Telephone Company v. linkLine Communications, No. 07-512 (U.S. Sup. Ct., Oct. 17, 2007)*. The Commission issued the statement in the interests of transparency. It can be found as a link to this press release on the Commission's Web site.

The plaintiff in linkLine alleged that defendant violated Section 2 of the Sherman Act when it used its alleged monopoly power in the wholesale market for DSL service to "squeeze" its downstream competitors in the retail DSL market by charging wholesale prices equal to, and at times higher than, its retail prices. The district court and the Ninth Circuit held that "price-squeeze" allegations in this case were sufficient to make out a claim under Section 2.

Appendix

In the Commission's statement, the FTC summarizes the case and the recent ruling by the Ninth Circuit, discusses its analysis of the issues presented, and concludes "[i]n sum, we do not believe this case is ripe for review by the Supreme Court. There is no apparent justification, based on only a partial record of the plaintiffs' pleadings in this case, for turning back 60 years of case law that embraces price-squeeze claims under Section 2 of the Sherman Act."

In the Commission's view, the Ninth Circuit's narrow decision does not conflict with the Court's antitrust jurisprudence and is consistent with Judge Hand's decision in *United States v. Aluminum Co. of America, 148 F.2d 416 (2nd Cir. 1945)* and Justice (then Judge) Breyer's decision in *Town of Concord v. Boston Edison Co., 915 F.2d 17 (1st Cir. 1990).* The Commission sees no reason to reject the latter jurisprudence, especially where, as here, the decision of the Ninth Circuit is consistent with those of the other courts of appeals that have addressed price-squeeze allegations, and the Court must credit the allegations of the amended complaint in any review.

The vote not to join the brief was 3-0, with Chairman William E. Kovacic recused.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about

particular business practices, call 202-326-3300, send an e-mail to antitrust@ftc.gov, or write to the Office of Policy and Coordination, Room 394, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave., N.W., Washington, DC 20580. To learn more about the Bureau of Competition, read "Competition Counts" at http://www.ftc.gov /competitioncounts.

Appendix

Statement of the Federal Trade Commission

Petition for a Writ of Certiorari in *Pacific Tel. Co. d/b/a AT&T California v. linkLine Comms., Inc.* (No. 07-512)

The Commission declines to join the U.S. Department of Justice in recommending that the U.S. Supreme Court review the Ninth Circuit's decision in *linkLine Comm'n v. Pacific Bell Telephone Co.*, 503 F.3d 876 (9th Cir. 2007), because we disagree with DOJ's analysis, and because this case does not appear to be worthy of review at this time. The vote was 3 - 0 with Chairman Kovacic recused. In the interests of transparency, this statement describes the reasons for the Commission's decision.

BACKGROUND

In 2003, linkLine filed a complaint alleging that Pacific Bell (d/b/a AT&T) had monopolized and attempted to monopolize the relevant DSL Internet services market, in violation of Section 2 of the Sherman Act, by, among other things, "creat[ing] a price squeeze by charging ISPs a high wholesale price in relation to the price at which defendants were providing retail services." Pet. App. 4a; Cmplt. ¶ 23(a). Pacific Bell moved for judgment on the pleadings on the ground that the Court's decision in *Verizon Comms. Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) compelled judgment in defendants' favor. The district court denied that motion, holding that "because a price-squeeze claim

is actionable under existing antitrust standards, and because the Ninth Circuit has upheld the viability of price-squeeze claims in the context of highly regulated industries, *Trinko* does not bar Plaintiffs' price-squeeze claim." Pet. App. 91a. However, it ordered plaintiffs to file an amended complaint "limited to the price-squeeze claim that details beyond the normal requirements of Rule 8 specific facts supporting Plaintiffs' price-squeeze claim." *Ibid.*

Respondents' amended complaint elaborated on the price-squeeze claim by providing the additional allegations that

> defendants * * * engag[ed] in an unlawful price squeeze by intentionally charging independent ISPs wholesale prices that were too high in relation to prices at which defendants were providing retail DSL services and necessary equipment to end-user customers — and for a period by charging wholesale DSL prices to competing ISPs (such as plaintiffs) that actually exceeded the prices at which defendants' retail affiliate (PBI) was charging retail end-user customers for DSL services and necessary equipment * * *.

Pet. App. 5a-6a; Am. Cmplt. ¶ 25(A)(1). Respondents alleged further that

> if defendants themselves charged their retail affiliates the same wholesale costs for DSL

> transport that they charged their wholesale ISP customers (such as plaintiffs), defendants could not cover their wholesale costs and make a profit from DSL service at their low retail prices for their bundled offering of DSL, Internet Service and necessary equipment * * *. Given the price margin relationship between retail and wholesale prices, defendants are clearly attempting to compensate for deliberately sacrificing profits on the retail end of their operations (with offsetting margins on the wholesale side) in order to stifle, impede and exclude competition from independent ISPs such as plaintiffs that are both wholesale customers and retail rivals.

Pet. App. 6a-7a; Am. Cmplt. ¶ 25(A)(3).

Pacific Bell moved to dismiss the price-squeeze claim in the amended complaint for failure to state a claim in accordance with the standards of *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). The district court denied that motion, holding that "even if the *Brooke Group* requirements were applied, the FAC [first amended complaint] would satisfy those requirements." Pet. App. 47a-48a. The district court then granted AT&T's motion to certify its earlier order regarding *Trinko*'s application to price-squeeze claims for interlocutory appeal pursuant to 28 U.S.C. § 1292. Pet. App. 56a, 8a. The district court noted, however, that in light of its holding that linkLine's

amended complaint satisfied *Brooke Group*'s dual conditions, "the issue before the Ninth Circuit will not only be whether *Trinko* bars price-squeeze claims generally but, more specifically, whether it bars predatory price-squeeze claims (i.e., price-squeeze claims which comply with the *Brooke Group* requirements)." Pet. App. 56a n.22.

The Ninth Circuit affirmed. It noted that price-squeeze claims were recognized under Section 2 of the Sherman Act long before the Supreme Court's *Trinko* decision.[1] Pet. App. 8a-9a (citing, among other decisions, *United States v. Aluminum Co. of America*, 148 F.2d 416, 437-38 (2nd Cir. 1945) ("*Alcoa*"); *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992). It then asked "whether *Anaheim* remains viable after *Trinko*," Pet. App. 13a, and concluded that several factors mandate that its own price-squeeze precedent survives the Supreme Court's decision. First, *Trinko* "took great care to explain that in this particular regulatory context, 'claims that satisfy established antitrust standards' are preserved." Pet. App. 14a (quoting 540 U.S. at 406). Thus, the price-squeeze claims that were recognized in *Anaheim*, and which "formed part of the fabric of traditional antitrust law" prior to *Trinko*, "should remain viable notwithstanding either the telecommunications statutes or *Trinko*." *Id.* Second,

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1. Price squeeze, said the Ninth Circuit, "occurs when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market." Pet. App. 8a (citation omitted).

both *Trinko* and *Anaheim* recognized that "courts should tread carefully" when dealing with allegedly anticompetitive conduct in regulated industries.[2]

Applying both *Trinko* and its own *Anaheim* decision, the Ninth Circuit noted that unlike the circumstances in those cases, the challenged conduct in the *linkLine* case concerned "a partially regulated industry." Pet. App. 16a. It emphasized that Federal Communication Commission regulation "applies only to the wholesale prices [AT&T] charged linkLine; there is no comparable regulatory attention paid to the retail DSL market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws." Pet. App. 18a. Thus, "since linkLine could prove facts, consistent with its complaint, that involve only unregulated behavior at the retail level, its action or lawsuit survives a motion for judgment on the pleadings." *Ibid.*

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2. *Trinko* declared that "the existence of a regulatory structure designed to deter and remedy anticompetitive harm" was *"[o]ne factor* of particular importance." Pet. App. 13a (citing *Trinko*, 540 U.S. at 412-14) (emphasis by the 9th Circuit). *Anaheim*, for its part, "carefully circumscribed" the price-squeeze theory by "requir[ing] a showing of specific intent on the part of the wholesale monopoly holder to 'serve its monopolistic purposes at [retail competitors'] expense' in order for § 2 liability to attach." Pet. App. 14a-15a (quoting *Anaheim*, 955 F.2d at 1378). The Ninth Circuit concluded that "[w]here * * * there is nothing built into the regulatory scheme which performs the antitrust function, the benefits of antitrust are worth its sometimes considerable disadvantages." *Ibid.* (quoting 540 U.S. at 412) (internal citation, quotation marks and alterations omitted).

Appendix

DISCUSSION

The holding of the Ninth Circuit is unquestionably correct, and indeed merely echoes what other courts of appeals have held on the narrow issue presented to the court below: that claims of a predatory price squeeze in a partially regulated industry remain viable after *Trinko*.[3]

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3. There is no real conflict between the narrow decision of the Ninth Circuit and the decisions of the two other courts of appeals that have considered price-squeeze claims in the wake of *Trinko* or between those two decisions. In *Covad Communications Co. v. BellSouth Corp.* ("*BellSouth*"), the Eleventh Circuit considered allegations substantially similar to those in linkLine's amended complaint, and held that the "price squeezing claim survives because it is based on traditional antitrust doctrine and is not specifically barred by *Trinko*." 374 F.3d 1044, 1050 (11th Cir. 2004). The D.C. Circuit considered the same issue in *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005) ("*Bell Atlantic*"). The court dismissed Covad's price-squeeze claim. On rehearing, the *Bell Atlantic* court emphasized that its holding was limited to non-predatory price-squeeze claims. 407 F.3d 1220 (D.C. Cir. 2005). It noted that Covad's argument that its holding "eliminates" price-squeeze claims entirely "simply misreads our opinion," which focused on the non-voluntary relationship between Covad and Bell Atlantic. *Id.* at 1222. It then distinguished its own facts from those in the Eleventh Circuit's decision upholding predatory price-squeeze claims: "Notably, the court did not face a circumstance similar to that in [*BellSouth*], in which the Eleventh Circuit held a claim for predatory pricing of loops could proceed. * * * Here, Covad did not argue its claim as one of price predation and, unsurprisingly, we did not treat it as such." *Ibid.*

It bears emphasis that the price-squeeze theory pleaded in *linkLine* is not novel. As the court of appeals noted, *Trinko* "took great care" to preserve "'claims that satisfy established antitrust standards'." Pet. App. 14a (quoting 540 U.S. at 406). Price-squeeze claims have long been part of the Section 2 doctrine, *see* Pet. App. 8a-9a. The price-squeeze theory pleaded in linkLine is similar to the theory first embraced by Judge Learned Hand in the Second Circuit's seminal opinion in the *Alcoa* case over sixty years ago. *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945). In *linkLine*, as in *Alcoa*, the defendant and the plaintiffs allegedly competed for retail customers, but plaintiffs alleged that the defendant enjoyed monopoly power over an essential input and had set wholesale prices for that input so high that plaintiffs could not profitably compete. *Compare linkLine*, 503 F.3d at 879, *with Alcoa*, 148 F.2d at 437-38.

The gravamen of the price squeeze found in *Alcoa* was that the downstream competitors could not make a "living profit" because they were squeezed between Alcoa's high price for ingot and its low price for sheet. Brief at 13. It has been suggested that the allegations in *Alcoa* were merely complaints about an insufficient margin by competitors and that the legality of the conduct turned on its effects on competitors rather than competition. Yet in *Alcoa*, the court took the price of Alcoa's ingot and its 'rolling' costs as a fair measure of costs and compared those costs to Alcoa's sheet prices. *Alcoa*, 148 F.2d at 437. It found that the margin was negative in many instances (that is, the costs exceeded

the price) and only barely positive in other instances (by a few pennies). *Id.* In light of these facts, we understand Judge Hand's reference to "living profit" to be a profit sufficient for participants in the second market to compete. We believe this is a limiting principle, which is at least as clear as the undefined "below-cost" standard in *Brooke Group.*

A number of courts since *Alcoa* have held that price-squeeze allegations may support liability under Section 2. For example, the First Circuit in *Town of Concord* identified several respects in which a price squeeze may have anticompetitive effects. *See Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 28 (1st Cir. 1990) (Breyer, C.J.) (distinguishing several authorities that "suggest that a price squeeze may be unlawful in the regulated electricity industry" partly on the ground that in every one of those cases, "the price-squeeze allegation involved wholesale prices that *exceeded* retail prices") (emphasis original).[4] Even accepting "'the widely accepted' (albeit 'counterintuitive') economic argument * * * that 'there is but one maximum monopoly profit to be gained from the sale of an end-product'," *id.* at 23 (citing 3 P. Areeda & D. Turner, *Antitrust Law* ¶ 725b, at 199 (1978)), the anticompetitive effects of a price-squeeze scheme can still be significant.

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4. Indeed, even the allegations in the seminal price-squeeze case arguably fall under the predatory pricing squeeze rubric. *See Alcoa*, 148 F.2d at 436-37 (using the sum of Alcoa's wholesale price of aluminum ingot plus its "rolling" costs as a fair measure of its downstream "costs," and comparing that with Alcoa's prices for aluminum sheet, finding the downstream margin to be negative in some instances).

The *Town of Concord* court pointed out at least two such harms: entrenching the monopoly in the upstream market, and eliminating non-price competition in the downstream market. *Id.* at 23-24. As to the first scenario, a monopolist in the upstream market can raise the costs of entry into that market by extending its dominance to the downstream market. A prospective upstream new entrant will thus be deterred not only by the pre-existing entry barriers but also by the prospect of having to compete on unequal terms with the incumbent because of the latter's control over the downstream market. "And insofar as the monopolist previously set prices cautiously to avoid attracting a competitive challenge, the added security of a two-level monopoly could even lead that monopolist to raise its prices." *Id.* at 24 (citing *Areeda & Turner* ¶ 725h, at 204-08; William G. Shepard, *Potential Competition Versus Actual Competition*, 42 ADMIN. L. REV. 5-34 (1990)). Likewise, even assuming no price effects from eliminating the downstream competition of an integrated monopolist, non-price competition in areas like quality and service can also be harmed by reducing the incentives for the monopolist to develop better products and more efficient means of production, and by eliminating the possibility of an independent downstream actor challenging the monopolist by developing better and more efficient downstream products. *See id.* (citing *Areeda & Turner*).

Furthermore, while in *Trinko*, *Town of Concord*, *BellSouth* and *Bell Atlantic* the conduct of the defendants was constrained by regulation, the existence of a regulatory regime in this case does not sufficiently

constrain AT&T's conduct, because the downstream or retail side of that market is unregulated. Thus, while the wholesale level is subject to "a series of regulatory mechanisms and regulatory agencies charged with assuring fair play," including, for example, "just, reasonable, and nondiscriminatory" pricing, Pet. App. 16a, 10a n.8, "[a]ny restrictions on pricing at the retail level derive primarily from the antitrust laws." Pet. App. 18a. Indeed, just such an anomaly was singled out by Justice (then Chief Judge) Breyer as an exception to the First Circuit rule that a non-predatory price squeeze in a fully regulated industry does not give rise to a claim under the Sherman Act. *See Town of Concord*, 915 F.2d at 29 ("We recognize that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first") (citing *Areeda & Turner* ¶ 726e, at 217-20 (1978)). Thus, the theory of price squeeze retains a significant role against anticompetitive unilateral conduct in a case like this and should not be summarily dismissed.

Moreover, as pleaded, this case does not undercut *Brooke Group*. The Supreme Court's stated concern in *Brooke Group* was that "false positives" may operate to deprive consumers of low prices. Assuming as true the allegations in linkLine's amended complaint, though, AT&T's retail pricing was predatory, and it was calculated to (and did) maintain monopoly power for AT&T in the retail market for DSL-based Internet access services. Thus, the plaintiffs in *linkLine* have

alleged that consumers have paid supracompetitive prices as a result of AT&T's conduct. On an appeal from plaintiffs' pleadings, it must be assumed that consumers have paid those prices.

Indeed, the fact that the case would come to the Court at the pleadings stage reinforces the impropriety of review. That procedural posture not only deprives the Court of a fully developed record, but adds a further layer of complexity to the proper legal question presented. One of the central issues in this case will be which measure of AT&T's wholesale costs is appropriate for predation analysis — a factual determination that has yet to be made by the district court. Thus, even if the Court goes beyond the actual question presented to consider the predation allegations in the amended complaint (with the attendant possibility for jurisdictional infirmity), it can hardly opine usefully on the issue without benefit of an appropriate measure of cost.

In sum, we do not believe this case is ripe for review by the Supreme Court. There is no apparent justification, based on only a partial record of the plaintiffs' pleadings in this case, for turning back 60 years of case law that embraces price-squeeze claims under Section 2 of the Sherman Act. The FTC and the Solicitor General frequently cooperate in fashioning recommendations to the Supreme Court regarding the grant or denial of certiorari, and likely will continue to do so.

AMICUS CURIAE BRIEF

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In the Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY,
DBA AT&T CALIFORNIA, ET AL., PETITIONERS

v.

LINKLINE COMMUNICATIONS, INC., ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether a plaintiff states a claim under Section 2 of the Sherman Act, 15 U.S.C. 2, by alleging that the defendant—a vertically-integrated retail competitor with an alleged monopoly at the wholesale level—engaged in a "price squeeze" by leaving an insufficient margin between wholesale and retail prices to allow the plaintiff to compete, when the defendant has no antitrust duty to provide the wholesale input to the plaintiff.

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In the Supreme Court of the United States

No. 07-512

PACIFIC BELL TELEPHONE COMPANY
DBA AT&T CALIFORNIA, ET AL., PETITIONERS

v.

LINKLINE COMMUNICATIONS, INC., ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS

INTEREST OF THE UNITED STATES

The Department of Justice is responsible for enforcing the federal antitrust laws and has a strong interest in the correct application of those laws. At the Court's invitation, the United States filed a brief as amicus curiae at the petition stage of this case.

STATEMENT

1. Petitioners are various affiliates of a dominant regional telephone company that provides telephone and data transmission services, including digital subscriber line (DSL) Internet service, to retail consumers over its telecommunications infrastructure and facilities. Respondents are Internet service providers (ISPs) that also sell DSL service at retail, in competition with petitioners. Pet. App.

2a-3a. Because petitioners own the requisite infrastructure and facilities, including local telephone lines (*id.* at 2a-3a & n.1), respondents leased "DSL transport" from petitioners on a wholesale basis.[1] Consequently, petitioners supplied respondents at wholesale with a necessary input to their DSL service and also competed with respondents in providing a "bundled package" of online service and equipment, including DSL service, to consumers. *Id.* at 2a-3a; see J.A. 17 (¶ 19); see also J.A. 12 (¶ 8) (petitioners sold Internet access service along with DSL); J.A. 13-14 (¶ 12) (listing various services incorporated into Internet service).

Petitioners did not supply respondents voluntarily, but rather because federal telecommunications law required them to do so. Pet. App. 5a n.6.[2] As the district court concluded (*id.* at 78a-85a), rules adopted by the Federal Communications Commission (FCC) pursuant to the Communications Act of 1934 obligated petitioners to offer respondents "nondiscriminatory access" to DSL transport at "just and reasonable" rates. *Id.* at 83a-84a (citing 47 U.S.C. 201; *Review of Regulatory Requirements for Incumbent LEC Broadband Telecomm. Servs.*, 17 F.C.C.R. 27,000, 27,010, ¶ 18 (2002); *Policy and Rules Concerning the Interstate, Interexchange Marketplace*, 16 F.C.C.R. 7418, 7445-7446, ¶ 46 (2001)).[3]

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[1] For industry technical and economic background, see Robert W. Crandall & Hal J. Singer, *Are Vertically Integrated DSL Providers Squeezing Unaffiliated ISPs (and Should We Care)?*, *in* Access Pricing: Theory and Practice 421, 424-440 (Ralf Dewenter & Justus Haucap eds., 2007).

[2] Respondents did not dispute that point on appeal. Pet. App. 5a n.6.

[3] For many local telephone companies, the FCC has eliminated the obligation to provide DSL transport as a condition of entering the market for DSL-based Internet-access service, in part because of the prevalence of other technologies (such as cable modem service) that provide similar high-speed Internet connections. See *Appropriate*

Respondents sued petitioners in July 2003, alleging monopolization and attempted monopolization of the regional DSL market in violation of Section 2 of the Sherman Act, 15 U.S.C. 2. See J.A. 10-24. Respondents alleged that petitioners had "created a price squeeze by charging [respondents] a high wholesale price in relation to the price at which [petitioners] were providing retail services," J.A. 18 (¶ 23(a)), and that this "price squeeze" placed respondents at a "serious unfair disadvantage," J.A. 17 (¶ 19). The district court described respondents' other allegations of improper conduct by petitioners, J.A. 19 (¶ 23(b)-(f)), as "refusal to deal" and "denial of access to an essential facility." Pet. App. 77a.

2. After this Court's decision in *Verizon Communications Inc.* v. *Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), petitioners moved for judgment on the pleadings, contending that *Trinko* compelled judgment in their favor. Pet. App. 65a. In an October 2004 order (2004 Order), the district court granted petitioners' motion as to respondents' refusal-to-deal and essential-facility allegations, *id.* at 77a-86a, 90a-91a, but denied the motion as to the price-squeeze claim, *id.* at 86a-91a.

The court held that *Trinko* did not "directly" bar a claim based on price-squeeze allegations, rejecting petitioners' argument that "a price squeeze claim is essentially a

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Framework for Broadband Access to the Internet over Wireline Facilities, 20 F.C.C.R. 14,853, 14,873 ¶ 33, 14,881-14,882 ¶ 51 (2005), petitions for review denied *sub nom.*, *Time Warner Telecom, Inc.* v. *FCC*, 507 F.3d 205 (3d Cir. 2007). As a condition of the FCC's approval of a recent merger, however, petitioners remain under an obligation to provide DSL transport at a price no higher than the retail rate they charge for retail DSL-based Internet-access service. See *AT&T Inc. & BellSouth Corp. Application for Transfer of Control*, 22 F.C.C.R. 5662, 5814-5815, App. F, on partial reconsideration on other grounds, 22 F.C.C.R. 6285 (2007).

refusal-to-deal claim," *i.e.*, "a claim that Firm One is refusing to deal with Firm Two on Firm Two's price terms." Pet. App. 86a. Although the court acknowledged that petitioners' argument "has a certain logic to it," the court rejected the argument on the ground that not all refusal-to-deal claims can "be reframed as price-squeeze claims." *Id.* at 86a-87a. The court also stated that, "to the extent that price-squeeze claims are subject to the requirements set forth in *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), [for predatory-pricing claims,] then the transmutability of refusal-to-deal claims is limited still more." *Ibid.*

The district court also rejected petitioners' argument that "price squeeze liability is inappropriate where, as here, wholesale prices are regulated by a federal regulatory agency." Pet. App. 87a-88a. The court observed that *Trinko* pointed to the "existence of a regulatory structure designed to deter and remedy anticompetitive harm" as a reason not to expand the scope of Section 2 liability. *Id.* at 88a (quoting *Trinko*, 540 U.S. at 412). The court concluded, however, that regulation of petitioners' wholesale prices was not determinative because, under governing Ninth Circuit precedent, the existence of a regulatory structure does not preclude antitrust liability for a price squeeze, *id.* at 88a-89a (citing *City of Anaheim* v. *Southern Cal. Edison Co.*, 955 F.2d 1373 (1992)), and such a claim "falls within the range of recognized Section 2 claims," *id.* at 90a. Accordingly, the court held that "*Trinko* does not bar [respondents'] price-squeezing claim." *Id.* at 91a.

The district court did not reach petitioners' "objections to the legal sufficiency of [respondents'] price-squeeze claim which [did] not derive from *Trinko*," Pet. App. 91a, including petitioners' argument that the complaint failed to satisfy the *Brooke Group* requirements—*i.e.*, allegations of pricing below an appropriate measure of costs and a dan-

gerous probability of recoupment. See 03-5265 Mem. in Supp. of J. on Pleadings 15. The court instead ordered respondents to file an amended complaint detailing the specific facts supporting their price-squeeze claim. Pet. App. 91a.

3. Respondents filed an amended complaint (J.A. 25-42), and petitioners then moved to dismiss it, arguing *inter alia* that price-squeeze claims must satisfy the *Brooke Group* requirements and that the amended complaint failed to do so. Pet. App. 36a. In an April 2005 order (2005 Order), the district court denied that motion. *Id.* at 25a-57a. Although the court found the "policy arguments" for applying the *Brooke Group* requirements "persuasive," *id.* at 47a, the court concluded that it was unnecessary to resolve that "difficult issue" because it concluded that the amended complaint would satisfy the *Brooke Group* requirements when "generously construed" in accordance with the "no set of facts" standard of *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957). Pet. App. 49a, 56a.

The district court granted petitioners' alternative request to amend the 2004 Order to certify it for interlocutory appeal pursuant to 28 U.S.C. 1292(b), identifying the "controlling question of law" as "whether *Trinko* bars price squeeze claims in a fully regulated industry" in which "the parties are compelled to deal under the federal communications laws." Pet. App. 53a, 56a-57a. The court stated that "the issue before the Ninth Circuit will not only be whether *Trinko* bars price squeeze claims generally but, more specifically, whether it bars predatory price squeeze claims (i.e., price squeeze claims which comply with the *Brooke Group* requirements)." *Id.* at 56a n.22.[4]

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[4] No single district court order contains both the statutory certification requirements and the order certified in haec verba. Cf. 28 U.S.C. 1292(b) (providing that district court's finding requisite to appeal

4. The court of appeals granted permission to appeal, Pet. App. 92a, and a divided panel affirmed, *id.* at 1a-24a.

a. The panel majority framed the question presented as whether *Trinko* bars price-squeeze claims against a defendant "who has no duty to deal with the plaintiff absent statutory compulsion." Pet. App. 1a. The majority explained that a price squeeze occurs "when a vertically integrated company sets its prices or rates at the first (or 'upstream') level so high that its customers cannot compete with it in the second-level (or 'downstream') market." *Id.* at 8a (quoting 2 Julian O. von Kalinowski et al., *Antitrust Laws and Trade Regulation* § 27.04[1], at 27-40 (2d ed. 2007)). It stated that federal courts have recognized the viability of such price-squeeze claims under the Sherman Act since *United States* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945). Pet. App. 8a-9a. The panel majority declined to reconsider, and instead reaffirmed, the Ninth Circuit's *Anaheim* decision, which held that price-squeeze claims are "viable against monopolists in regulated industries" if the plaintiff proves "specific intent on the part of the wholesale monopoly holder." *Id.* at 9a, 14a.

The majority reasoned that "*Trinko* did not * * * completely eliminate the viability of a § 2 price squeeze theory in regulated industries." Pet. App. 15a. To the contrary, the majority concluded that *Anaheim* was "consis-

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pursuant to the provision shall be "state[d] in writing in" the order certified for appeal). However, as explained in the United States's brief at the petition stage (at 18-19), by granting petitioners' motion to "amend this Court's October 20, 2004 Order to certify for interlocutory review so much of the Order as permits [respondents'] price-squeeze claim to proceed," 03-5265 Mot. to Strike, Dismiss, or Certify 1, the district court necessarily granted the request to amend the 2004 Order as the statute requires. See, *e.g.*, Fed. R. App. P. 5(a)(3) ("the district court may amend its order * * * to include the required permission or statement"); *In re Hamilton*, 122 F.3d 13, 14 (7th Cir. 1997).

tent with *Trinko*" in "reject[ing] the wholesale importation of antitrust theory as applicable to regulated industries." *Ibid.* The majority stated that in "any future application of *Anaheim*" the court would "ensure consistency with *Trinko*." *Id.* at 16a.

Applying *Anaheim* and *Trinko*, the court upheld the district court's denial of judgment on the pleadings. Pet. App. 16a-19a. It emphasized that the FCC regulates only "the wholesale prices [petitioners] charged [respondents]; there is no comparable regulatory attention paid to the retail DSL market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws." *Id.* at 18a. The court stated that it was "unclear at this juncture the extent to which [respondents are] basing [their] § 2 price squeezing theory on wholesale pricing, retail pricing, or both." *Ibid.* But, "since [respondents] could prove facts, consistent with [their] complaint, that involve only unregulated behavior at the retail level, [their] action or lawsuit survives a motion for judgment on the pleadings." *Ibid.* The court thus concluded that the price-squeeze allegation "states a potentially valid claim" under Section 2. *Id.* at 19a.

b. Judge Gould dissented, concluding that the district court should have dismissed the amended complaint in its entirety. Pet. App. 19a-24a. In his view, *Trinko* "takes the issues of wholesale pricing out of the case, and thus transforms what is left of any claim of 'price squeeze.'" *Id.* at 20a. Therefore, he concluded, "the retail side of a price squeeze cannot be considered to create an antitrust violation if the retail pricing does not satisfy the requirements of *Brooke Group*." *Id.* at 23a. Judge Gould concluded that the amended complaint did not satisfy that standard, although he found "just enough possibility of an injury" to

warrant permitting respondents a further opportunity to amend the complaint. *Id.* at 23a, 24a n.2.[5]

SUMMARY OF ARGUMENT

The court of appeals erred in recognizing a claim under Section 2 of the Sherman Act based solely on allegations that a vertically-integrated company with an alleged monopoly at the wholesale level, but with no antitrust duty to provide that wholesale input to its retail competitors, engaged in a "price squeeze" by leaving an insufficient margin between wholesale and retail prices to allow its retail competitors to compete.

A. In the absence of an antitrust duty to deal, an allegation that a vertically-integrated defendant's wholesale prices are too high in relation to its retail prices for retail-level rivals to compete does not allege a claim under Section 2 of the Sherman Act. As this Court held in *Verizon Communications Inc.* v. *Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), a statutory or regulatory requirement to deal with rivals does not automatically establish an *anti-*

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[5] The court of appeals discussed both the 2004 and 2005 Orders and, in its paragraph summarizing the 2005 Order, stated that the district court certified "the order" for interlocutory appeal. Pet. App. 8a. In the end, however, it affirmed the district court's denial of petitioners' "motion for judgment on the pleadings," *id.* at 19a, which was the ruling in the 2004 Order, not the 2005 Order.

As explained in the government's brief at the petition stage (at 17-19), it could be argued that both the 2004 and 2005 orders were properly before the court of appeals. Regardless of whether the 2005 Order was properly before the court of appeals, however, that court did have jurisdiction to review the propriety of the 2004 Order denying petitioners' motion for judgment with respect to the original complaint. See note 4, *supra*. The court resolved that issue in favor of respondents, holding that price-squeeze claims remain viable after *Trinko* and that the Ninth Circuit's recognition of such claims in *Anaheim* in the context of regulated industries remains good law. Pet. App. 8a-16a. This Court possesses jurisdiction to review those holdings.

trust duty to deal. Because petitioners had no antitrust duty to deal with respondents at the wholesale level, petitioners had no duty under the antitrust laws to provide respondents with any particular wholesale price terms. Accordingly, respondents' claim that petitioners' wholesale prices were too high for respondents to compete at retail fails to state a Section 2 claim.

B. Nor is respondents' allegation that petitioners' retail prices are too low for them to compete sufficient to state a claim under Section 2. To state a claim based on petitioners' retail prices, respondents would have to allege the two requirements established by this Court for predatory-pricing claims: (1) that petitioners' retail prices are below an appropriate measure of their costs, and (2) that petitioners have a dangerous probability of recouping their investment in below-cost prices. See *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). In the absence of any such allegations, the antitrust laws risk punishing the very conduct they are designed to protect: vigorous price competition on the merits.

C. The Ninth Circuit erred in allowing respondents to proceed on their claims in the absence of an antitrust duty to deal or predatory-pricing allegations. A claim based solely on the assertedly insufficient margin between a vertically-integrated defendant's wholesale and retail prices would protect competitors, not competition or consumers. Low retail prices benefit consumers, regardless of how they are set, as long as they are above predatory levels. And a monopolist's high wholesale price is generally not in itself unlawful because, as this Court has recognized, collecting a monopoly profit is part of the free-market system.

In permitting respondents' price-squeeze claim to proceed, the Ninth Circuit relied on *United States* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945). But that

decision—which recognized a price-squeeze claim based on the notion that the vertically-integrated defendant charged more than a "fair price" for an upstream input such that its downstream rivals could not make a "living profit"—reflects an improper focus on the protection of competitors. Recognizing such a claim would displace the free-market price-setting mechanism and would place the antitrust court in the role of rate-setter, requiring it in most situations either to hold down the upstream price or impose a supracompetitive downstream price. Antitrust courts are ill-suited for that role.

ARGUMENT

Section 2 of the Sherman Act does not provide a cause of action for price-squeeze claims of the type at issue here—namely, allegations that a vertically-integrated company, with no antitrust duty to deal with its competitors, "created a price squeeze by charging [its retail competitors] a high wholesale price in relation to the price at which [it was] providing retail services," J.A. 18 (¶ 23(a)), such that it placed its competitors at a "serious unfair disadvantage," J.A. 17 (¶ 19). To accept such a price-squeeze theory, and thus premise antitrust liability on an assertedly inadequate margin between a defendant's wholesale and retail prices, would recognize an antitrust claim involving no allegations of conduct that harms competition in a way the antitrust laws forbid. Such a theory of liability cannot be reconciled with this Court's modern antitrust jurisprudence or the sound principles on which that jurisprudence is based. In particular, this Court's decision in *Trinko* forecloses respondents' claims that petitioners' wholesale prices are too high. And respondents' claim that petitioners' retail prices are too low cannot survive in the absence of allegations satisfying the requirements for a predatory-pricing claim set forth by this Court in *Brooke Group*. Despite the absence of such

allegations, the court of appeals allowed respondents' complaint to proceed. That erroneous decision threatens to chill retail price-cutting by vertically-integrated firms and to encourage litigation designed to protect competitors at the expense of competition, thereby undermining the procompetitive purposes of the antitrust laws and harming consumers.

A PRICE-SQUEEZE ALLEGATION BASED SOLELY ON THE MARGIN BETWEEN A VERTICALLY-INTEGRATED DEFENDANT'S WHOLESALE AND RETAIL PRICES IS INSUFFICIENT TO STATE A CLAIM UNDER SECTION 2 OF THE SHERMAN ACT

A. Absent An Antitrust Duty To Deal, A Claim That A Vertically-Integrated Defendant's Wholesale Prices Are Too High For Rivals To Compete At Retail Does Not Allege A Section 2 Claim

1. In *Trinko*, this Court held that allegations of insufficient assistance to rivals by a dominant telecommunications carrier with respect to services required by the telecommunications laws did not state a claim under Section 2 of the Sherman Act. 540 U.S. at 407-416. In that case, the plaintiff claimed that Verizon had breached its duties under the telecommunications laws by "fill[ing] rivals' orders on a discriminatory basis as part of an anticompetitive scheme to discourage customers from becoming or remaining customers" of its rivals, thus impeding rivals' "ability to enter and compete in the market for local telephone service." *Id.* at 404.

In rejecting that claim, the Court first held that a statutory and regulatory requirement to deal with rivals does not automatically establish a duty to deal for purposes of the antitrust laws. *Trinko*, 540 U.S. at 405-407. Rather, the Court reasoned, if the allegation that Verizon denied inter-

connection services to rivals in order to limit entry "state[d] an antitrust claim at all, it [did] so under § 2 of the Sherman Act." *Id.* at 407. And the Court concluded that such an allegation did not state a Section 2 claim, holding that Verizon had no antitrust duty to assist its rivals in the circumstances of that case. *Id.* at 407-416.

In so holding, the Court distinguished *Aspen Skiing Co.* v. *Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), describing that decision as "at or near the outer boundary of § 2 liability." *Trinko*, 540 U.S. at 409. In *Aspen*, the Court held that a particular refusal to deal with a competitor amounted to exclusionary conduct. 472 U.S. at 605-611. There, the defendant (which owned three of the four mountain areas in the Aspen ski area) and the plaintiff (which owned the fourth mountain area) had cooperated for years in the issuance of a joint ski ticket. After repeatedly demanding an increased share of the profits, the defendant refused to continue to participate in the joint ticket, even refusing to sell its tickets to the plaintiff at retail prices. *Id.* at 593-594.

Contrasting those facts with the allegations in *Trinko*, the *Trinko* Court emphasized the absence of any allegation that Verizon "voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion." 540 U.S. at 409. *Trinko* thus held that "Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents." *Id.* at 410.

The Court further concluded that "traditional antitrust principles" did not justify expanding "the few existing exceptions from the proposition that there is no duty to aid competitors," especially given "the existence of a regulatory structure designed to deter and remedy anticompetitive harm." *Trinko*, 540 U.S. at 411-412. Moreover, the Court noted that conduct constituting an anticompetitive breach

of the telecommunications laws may be "beyond the practical ability of a judicial tribunal to control." *Id.* at 414 (quoting *Brooke Group*, 509 U.S. at 223). The Court explained that "[e]ffective remediation of violations of regulatory sharing requirements will ordinarily require continuing supervision of a highly detailed decree." *Id.* at 414-415. And it concluded that "[n]o court should impose a duty to deal that it cannot explain or adequately and reasonably supervise." *Id.* at 415 (quoting Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 Antitrust L.J. 841, 853 (1989)).

2. Like the claims in *Trinko*, respondents' price-squeeze allegations amount to nothing more than a claim that petitioners refused to deal on terms that respondents desired. Respondents' original complaint was based on the allegedly "high wholesale price" that petitioners charged respondents "in relation to the price at which [petitioners] were providing retail services." J.A. 18 (¶ 23(a)).[6] But as the case comes to this Court, petitioners had no antitrust duty to deal with respondents at the wholesale level (see Pet. App. 1a, 85a), and thus no *antitrust* duty to provide respondents with any particular wholesale price terms. Rather, like the interconnection services Verizon provided in *Trinko*, petitioners provided DSL transport to respondents only under compulsion of the telecommunications laws. *Id.* at 5a n.6, 77a-85a.[7]

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[6] Because the district court assessed only the viability of the original complaint in the 2004 Order (which is the only order the district court unambiguously certified for appeal, see notes 4-5, *supra*), the discussion in text focuses on that complaint. The analysis would be the same if the allegations of the amended complaint were considered, because those allegations likewise turn on the allegedly insufficient margin between wholesale and retail prices. Pet. App. 5a-8a.

[7] In opposition to the certiorari petition, respondents argued that petitioners had an antitrust duty to deal cognizable under *Aspen*, based

From the standpoint of federal antitrust law, therefore, there would be no antitrust violation if petitioners refused to deal with respondents altogether (and thereby barred them from the retail market entirely). It necessarily follows that there can be no valid price-squeeze claim based merely on allegations that petitioners charged "wholesale prices that were too high in relation to what petitioners were charging their retail DSL customers" (Br. in Opp. 1), because that conduct amounts to nothing more than a refusal to deal with respondents on advantageous terms. A defendant that has no duty to deal with rivals by definition has no duty to deal with them on particular terms that would permit them to compete.[8]

Moreover, as this Court recognized in *Trinko*, the antitrust laws should not be used to enforce what boils down to a regulatory obligation to deal. Petitioners are obligated to offer respondents DSL transport at just, reasonable, and nondiscriminatory rates, and the FCC has authority to enforce that obligation with respect to petitioners' wholesale rates. See pp. 2-3, *supra*. As this Court recognized in *Trinko*, an "antitrust court is unlikely to be an effective

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on the contention that petitioners had "refus[ed] to provide competitors the same services or prices made available to their retail customers." Br. in Opp. 24. Neither the court of appeals nor the district court addressed that argument, presumably because the complaint contains no suggestion that respondents ever sought, or desired, to purchase from petitioners the bundled Internet access service (incorporating DSL transport) that petitioners sold at retail. See J.A. 12, 13-14, 17 (¶¶ 8, 12, 19). In any event, that issue is not fairly encompassed within the question presented, which explicitly assumes "no antitrust duty to provide the wholesale input to competitors." Pet. i.

[8] Indeed, even if a plaintiff could properly allege in a particular case that the defendant's pricing did constitute a breach of an antitrust duty to deal, characterizing that pricing as creating a "price squeeze" would add nothing to the allegation of an anticompetitive refusal to deal.

day-to-day enforcer" of the detailed obligations of the telecommunications laws. 540 U.S. at 415.

Petitioners suggest (Pet. Br. 35-37) that the existence of regulatory oversight provides an additional reason not to recognize a price-squeeze claim in this context. But there is no need for the Court to reach that argument. Regulatory enforcement should not displace antitrust enforcement unless the criteria for implied immunity are satisfied. The key point here is that, with or without a regulatory scheme, the antitrust laws should not be construed to forbid a mere margin-based price squeeze, because such a prohibition would represent unsound antitrust policy and conflict with this Court's modern antitrust jurisprudence. Accordingly, respondents' allegations that the margin between petitioners' wholesale and retail prices impeded their ability to compete (J.A. 17, 18 (¶¶ 19, 23(a)); Br. in Opp. 1) fare no better than the similar allegations regarding the provision of inadequate wholesale services in *Trinko*.

B. A Claim That A Vertically-Integrated Defendant's Retail Prices Are Too Low For A Rival To Compete At Retail Does Not State A Section 2 Claim In The Absence of Predatory-Pricing Allegations

1. Given that respondents' allegations regarding petitioners' wholesale prices do not furnish a basis for a claim under Section 2 of the Sherman Act, any antitrust claim arising out of petitioners' pricing would have to be based on their retail prices. But to allege a viable Section 2 claim based on retail prices, it would not be enough for respondents to claim that petitioners' retail prices were too low for respondents to compete. As this Court explained in *Brooke Group*, when "the essence of the claim" under Section 2 is that a "business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the

relevant market," "two prerequisites" must be met. 509 U.S. at 222. The plaintiff must prove that (1) "the prices complained of are below an appropriate measure of its rival's costs," *ibid.*, and (2) "the competitor had * * * a dangerous probability[] of recouping its investment in below-cost prices," *id.* at 224.[9]

In establishing that two-pronged standard, the Court reiterated its rejection of "the notion that above-cost prices that are below general market levels or the costs of a firm's competitors inflict injury to competition cognizable under the antitrust laws." *Brooke Group*, 509 U.S. at 223 (citing *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U.S. 328, 340 (1990)). As the Court explained, the below-cost-pricing prong is necessary because "[l]ow prices benefit consumers regardless of how those prices are set," *id.* at 223 (quoting *Atlantic Richfield*, 495 U.S. at 340), and when a company sets its price above the cost of its product, a low price often "reflects the lower cost structure of the alleged predator, and so represents competition on the merits." *Ibid.* The Court also emphasized the importance of the recoupment prong, observing that price cutting that does not result in recoupment produces lower prices in the market, thereby actually enhancing consumer welfare. *Id.* at 224.

2. Here, respondents' original complaint nowhere alleged that petitioners' retail prices were below an appropriate measure of petitioners' costs, or that there was a dangerous probability of recoupment. Hence, respondents do not contend, and there is no basis for suggesting, that the

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[9] Although *Brooke Group* involved a claim for primary-line price discrimination under the Robinson-Patman Anti-Discrimination Act, 15 U.S.C. 13(a), rather than a predatory pricing claim under Section 2 of the Sherman Act, the Court made clear that the same "two prerequisites to recovery" apply "whether the claim alleges predatory pricing under § 2 of the Sherman Act or primary-line price discrimination under the Robinson-Patman Act." 509 U.S. at 222.

original complaint alleged the elements of a predatory-pricing claim under *Brooke Group*. See *Brooke Group*, 509 U.S. at 222-224.

Although respondents contended in opposing certiorari (Br. in Opp. 14) that they have alleged a claim of "predatory" pricing, that contention is based on allegations in the amended complaint. The district court concluded in its 2005 Order that those allegations were sufficient to satisfy the *Brooke Group* requisites if "generously construed." Pet. App. 56a. As noted above (note 5, *supra*), however, it is unclear whether the 2005 Order and the amended complaint are properly at issue in this interlocutory appeal. And even if the amended complaint and the 2005 Order are properly at issue, the amended complaint's allegations are insufficient to satisfy *Brooke Group*.[10]

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[10] As the dissenting judge below correctly concluded (without any expression of disagreement from the majority), the amended complaint "does not allege" either that petitioners priced their retail product "below cost" or that petitioners "had any realistic prospect of recouping losses." Pet. App. 20a. Indeed, even the district court acknowledged that, "strictly construed, the [amended complaint] falls short in a number of respects," *id.* at 49a, noting that it lacks a factual allegation that "[petitioners'] prices are below a relevant measure of [petitioners'] costs," *id.* at 50a, and lacks an allegation of "a dangerous probability of recoupment within the meaning of *Brooke Group*," *id.* at 51a-52a. Instead, the amended complaint contains only a "conditional if-then statement" that "approximat[es]" an allegation of below-cost pricing, *id.* at 50a, and "something akin to" an allegation of recoupment, *id.* at 51a-52a. See J.A. 34-36 (¶ 25(A)(1)-(3)). In concluding that those allegations were nevertheless sufficient to satisfy *Brooke Group*, the district court relied on the proposition that dismissal is inappropriate unless "the plaintiff can prove no set of facts" that "would entitle him to relief." Pet. App. 49a (quoting *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957)). That view of the applicable pleading requirements, of course, was subsequently repudiated by this Court in *Bell Atlantic Corp.* v. *Twombly*, 127 S. Ct. 1955, 1969 (2007).

More to the point, whether or not respondents have a predatory-pricing claim that would satisfy the *Brooke Group* criteria, their claim is valid in the Ninth Circuit, because that court does not require satisfaction of those criteria. The court of appeals did not address the sufficiency of respondents' allegations under *Brooke Group* or hold that price-squeeze claims must satisfy the *Brooke Group* standard in order to survive a motion to dismiss. Indeed, the majority did not even discuss the subject of "predatory" pricing at any point in its opinion, notwithstanding the dissent's extended analysis of that issue. As explained below, the Ninth Circuit erred in allowing respondents to proceed on such a claim.

C. The Ninth Circuit Erred In Recognizing A Claim Under Section 2 Based Solely On The Margin Between A Vertically-Integrated Defendant's Wholesale And Retail Prices

Despite the absence of either an antitrust duty to deal or an allegation of predatory pricing, the Ninth Circuit allowed respondents to proceed on their complaint. In the Ninth Circuit's view, "[b]ecause a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." Pet. App. 14a. Some lower federal courts have "recognized price squeeze allegations as stating valid claims under the Sherman Act," *id.* at 8a-9a, beginning with *United States* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) (*Alcoa*). Like the "'essential facilities' doctrine crafted by some lower courts," *Trinko*, 540 U.S. at 410, however, the price-squeeze theory of antitrust liability has never been recognized by this Court. The Ninth Circuit erred in reaffirming the viability of pure price-squeeze claims in the circumstances here. *Trinko* and *Brooke Group*, and the sound antitrust principles on which they are based, combine

to bar price-squeeze claims that are based solely on the margin between an integrated defendant's wholesale and retail prices.

1. As this Court's cases make clear, in the absence of anticompetitive conduct, Section 2 does not condemn unilateral action that disadvantages a rival. See, *e.g.*, *Trinko*, 540 U.S. at 407 (monopolization); *Spectrum Sports, Inc.* v. *McQuillan*, 506 U.S. 447, 456-460 (1993) (attempted monopolization). Whether one competitor inflicts "painful losses" on another "is of no moment to the antitrust laws if competition is not injured," because "[i]t is axiomatic that the antitrust laws were passed for 'the protection of *competition*, not *competitors*.'" *Brooke Group*, 509 U.S. at 224 (quoting *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 320 (1962)); see *Weyerhaeuser Co.* v. *Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1077-1078 (2007). Even a firm with monopoly power has no general duty under the antitrust laws to assist its rivals. See *Trinko*, 540 U.S. at 407-409.

A price-squeeze theory focused solely on the margin between a vertically-integrated firm's retail price and the wholesale price at which it sells an essential input to retail competitors, see Pet. App. 8a, is inconsistent with those principles. As a leading antitrust treatise explains, "[m]ost" price squeezes are not "invidious." 3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c at 126 (2d ed. 2002) (*Antitrust Law*); see *ibid.* (observing that "it is difficult to see any *competitive* significance apart from the consequences of vertical integration itself, which may be adverse, neutral, or beneficial").

As this Court reiterated in *Brooke Group*, 509 U.S. at 223, a low retail price is ordinarily benign or procompetitive because "[l]ow prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition." *Atlantic Richfield*, 495 U.S. at 340. This Court has adhered to that

principle "regardless of the type of antitrust claim involved." *Ibid.* By the same token, a high upstream price is ordinarily lawful because the "charging of monopoly prices[] is not only not unlawful; it is an important element of the free-market system." *Trinko*, 540 U.S. at 407.[11] Indeed, price squeezes may occur "even in perfectly competitive markets" as a result of changing cost or demand conditions, particularly when an upstream product is a component of multiple downstream products facing different demand conditions. 3A *Antitrust Law* ¶ 767c at 127.

A price squeeze may disadvantage rivals, but as then-Judge Breyer explained for the First Circuit, "[m]erely eliminating competitors is not necessarily anticompetitive." *Town of Concord* v. *Boston Edison Co.*, 915 F.2d 17, 23 (1990), cert. denied, 499 U.S. 931 (1991).[12] In particular,

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[11] For that reason, even if a monopolist might have an antitrust duty to deal with his downstream competitors in particular circumstances, it would not necessarily follow that it must deal at less than the monopoly price. Yet if downstream competitors must pay monopoly prices for an important component of what they sell while competing against the monopolist, whose cost to produce that input is below the monopoly price, they are likely to face a margin-based price squeeze.

[12] In *Town of Concord*, the First Circuit declined to recognize a price-squeeze claim in a fully-regulated industry. 915 F.2d at 25-29. But the court did not uncritically accept the viability of a price-squeeze claim even in an unregulated market. It noted that to reach the conclusion that "the price squeeze is exclusionary, one must believe that the anticompetitive risks associated with a price squeeze outweigh the possible benefits and the adverse administrative considerations." *Ibid.* The court did not endorse that belief, however. It noted only that it did not question that conclusion in *Town of Concord* itself, but rather qualified it by observing that "the harms and benefits" of a price squeeze are "closely balanced." *Id.* at 25. The court's evident doubts about such a theory foreshadowed subsequent decisions of this Court that make clear that recognizing a price-squeeze claim based solely on the margin between a vertically-integrated defendant's wholesale and retail prices is inconsistent with the goals of antitrust law.

there are "at least two traditional circumstances in which prices that create a squeeze might simultaneously bring about economic benefits." *Id.* at 24. First, the upstream monopolist may be more efficient downstream than its downstream competitors. The squeeze may be attributable to the lower downstream prices brought about by that greater efficiency. *Ibid.*

Second, the upstream monopolist's entry into the downstream market, even if accompanied by a price squeeze, should lead to lower downstream prices if the downstream market was also characterized by monopoly before that entry. *Town of Concord*, 915 F.2d at 24. The downstream price is higher with two separate, successive monopolists than with a single monopolist over both markets. *Ibid.* By essentially the same logic, downstream prices may decline when the competing products in the downstream market are differentiated (*i.e.*, similar but not identical), and, after engaging in a price squeeze, the upstream monopolist then sells not only its own product but the product of the squeezed-out competitor. See Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct?*, 4 J. Competition L. & Econ. 271, 276 (2008).

2. In allowing respondents' price-squeeze claim to survive, the Ninth Circuit relied (Pet. App. 8a-9a), as have other lower courts, on the Second Circuit's decision in *Alcoa*. See, *e.g.*, *Town of Concord*, 915 F.2d at 18 (quoting *Alcoa*'s standard for finding price-squeeze liability and citing three post-*Alcoa* decisions "using substantially similar language" and reaching "the same conclusion"). But *Alcoa* reflects an improper (and, under this Court's decisions, outmoded) focus on the economic well-being of particular competitors, rather than on the protection of competition.

In *Alcoa*, the court of appeals, on certificate from this Court, concluded that Alcoa had violated Section 2 by monopolizing the manufacture and sale of virgin aluminum

ingot, from which sheet is made. 148 F.2d at 432. The *Alcoa* court then turned to the government's ancillary allegations, see *id.* at 422, including a price-squeeze claim. The gravamen of the alleged price squeeze was that independent sheet rollers, which purchased ingot mainly from Alcoa, were squeezed between the pincers of Alcoa's high price for ingot and the low price at which Alcoa itself sold sheet, and they therefore could not make a "living profit." *Id.* at 437.[13] The court deemed the conduct unlawful to the extent that the price of ingot was "higher than a 'fair price.'" *Id.* at 438.[14]

To determine whether Alcoa's ingot price was higher than a "fair price," the court took the price that Alcoa charged its competitors for ingot, added a "fair measure" of its competitors' costs of rolling the ingot into sheet (derived from Alcoa's costs of rolling sheet), and subtracted the sum from the price Alcoa charged for sheet, yielding a measure of the profit available to the independent rollers. *Alcoa*, 148

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[13] Independent fabricators of consumer products, such as cookware, made from aluminum sheet purchased on the open market, were also affected by the margin. As the *Alcoa* district court noted, while independent sheet rollers were complaining to Alcoa that the margin was too small, those independent fabricators, which competed against firms that were sheet rollers as well as fabricators of consumer products, were complaining to Alcoa that the margin was too large, leaving them at a competitive disadvantage in markets for consumer products made from aluminum. *United States* v. *Aluminum Co. of Am.*, 44 F. Supp. 97, 213-214 (S.D.N.Y. 1941), aff'd in part, rev'd in part, and remanded, 148 F.2d 416 (2d Cir. 1945). As the district court observed, Alcoa was subjected to a "cross-fire * * * by its competitors and customers." *Id.* at 213.

[14] The exercise of power that the court identified as wrongful was not charging too low a price for sheet, since "the 'squeeze' was eliminated by lowering the price of ingot" beginning in 1933, *Alcoa*, 148 F.2d at 437, rather than by raising the price of sheet.

F.2d at 437.[15] On this basis, the court concluded that Alcoa's pre-1933 prices for ingot were higher than a "fair price," because the profit available to competitors was small or, in some instances, nonexistent. *Ibid.*

The *Alcoa* court acknowledged that the high ingot price was "a consequence of" Alcoa's ingot monopoly, lawful or unlawful, "and perhaps * * * ought not to be considered as a separate wrong." 148 F.2d at 438. Moreover, the court did not "use it as part of the reasoning by which [it] conclude[d] that the monopoly was unlawful." *Ibid.* The court also "assent[ed] to the [district court's] finding that [the price squeeze] was not part of an attempt to monopolize the 'sheet' market." *Ibid.* Nevertheless, the court concluded that setting the price of ingot too high for the independent rollers to earn a living profit was "an unlawful exercise of [Alcoa's] power." *Ibid.* The court thus treated the price squeeze as unlawful, without regard to its contribution to the acquisition or maintenance of monopoly power or its relationship to any attempt to monopolize. That reasoning, which applied Section 2 to unilateral conduct that was neither monopolization nor attempted monopolization, was "incorrect." 3A *Antitrust Law* ¶ 767d2, at 131. See *Trinko*, 540 U.S. at 415 n.4 (rejecting a monopoly leveraging theory, noting that "[t]o the extent the Court of Appeals dispensed with a requirement that there be a 'dangerous probability of success' in monopolizing a second market, it erred").

In addition, the concepts on which *Alcoa* relied—"fair price," a price too high to allow downstream competitors a

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[15] It did this for various types and gauges of sheet for the years 1925-1933. For 31 of the 112 computations, there was no available profit. Concluding Alcoa increased the margin beginning in 1933 out of fear of "action by the Department" of Justice, the court performed similar computations for 1933-1937, yielding much higher average available profit figures. *Alcoa*, 148 F.2d at 437.

"living profit," or one too high to allow them to compete—are vague, imprecise, and can be unmeasurable. See *Town of Concord*, 915 F.2d at 25. But the flaw in *Alcoa*'s approach goes beyond difficulties in administration: it lacks any clear relationship to protecting marketplace competition or consumer welfare. A legal rule that requires a vertically-integrated defendant to charge wholesale and retail prices that ensure its rivals—regardless of their efficiency—a "fair price" or "living profit" protects competitors, not competition or consumers. Under this Court's cases, however, a firm's conduct may not be judged anticompetitive, predatory, or exclusionary "by simply considering its effect on" competitors. *Aspen*, 472 U.S. at 605.

Moreover, in most situations, mitigating a squeeze through application of the antitrust laws would require interference with the free-market price-setting mechanism ordinarily protected by those laws. In particular, such a forced increase of the margin between the defendant's wholesale and retail prices would entail the substitution of judicial regulation of prices for the market in one of two ways: either by holding down the upstream price or by requiring "firms to maintain supracompetitive prices" downstream, "thus depriving consumers of the benefits of lower prices." *Brooke Group*, 509 U.S. at 224. But an antitrust court is unlikely to be an effective rate-setter, much less "an effective day-to-day enforcer" of such rates. *Trinko*, 540 U.S. at 415; see *Town of Concord*, 915 F.2d at 25 (observing that "antitrust courts normally avoid direct price administration"). Rather, any anticompetitive effects from a price squeeze are likely to be "beyond the practical ability of a judicial tribunal to control." *Brooke Group*, 509 U.S. at 223.[16]

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[16] Contrary to the Federal Trade Commission's (FTC) suggestion (see Resp. Supp. Cert. Br. 10a-11a & n.4), *Alcoa*'s "available profit" cal-

3. To be sure, there may be cases in which a defendant's prices are set for exclusionary purposes, but no antitrust liability would arise under the combined holdings of *Trinko* and *Brooke Group* because the defendant has neither violated an antitrust duty to deal nor priced below cost. Indeed, the Court expressly recognized in *Brooke Group* that its standard might permit some anticompetitive price-cutting, *i.e.*, price-cutting that would exclude rivals on a basis other than efficiency. Specifically, the Court observed that above-cost pricing could sometimes be used "to induce or reestablish supracompetitive pricing," *Brooke Group*, 509 U.S. at 224, and implicitly acknowledged that, even absent recoupment, below-cost pricing could allow a predator to establish short-term market power by injuring and driving out its rivals—until new competitors entered the

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culations bear no relation to the *Brooke Group* requirement of below-cost pricing. The *Brooke Group* standard would have required consideration of whether Alcoa's price for sheet was below *Alcoa*'s total cost of producing sheet—which included not only Alcoa's cost of rolling ingot into sheet (which the Second Circuit did consider) but also Alcoa's cost of producing ingot. To perform that calculation, the Second Circuit would have needed to know Alcoa's cost of producing ingot. But, as the district court observed, the government did not "introduce in evidence the facts showing the cost of producing ingot." *Alcoa*, 44 F. Supp. at 219. Thus, instead of measuring whether Alcoa sold sheet below any relevant measure of its actual cost of producing sheet, the Second Circuit compared Alcoa's price for sheet with its *rivals'* cost of producing sheet. The rivals' cost, however, necessarily included not only their costs of rolling ingot into sheet, but also the monopoly price that they paid to Alcoa for ingot—a monopoly price that was not in itself unlawful. The Second Circuit therefore measured the wrong thing: by comparing Alcoa's price for sheet with its rivals' cost of producing sheet, it merely demonstrated that the rivals were indeed squeezed. It did not demonstrate the existence of conduct that, under this Court's modern antitrust jurisprudence, the antitrust laws were designed to prevent.

market and drove the market price back down. *Id.* at 224-225.

But whether or not such prices are the downstream component of a price squeeze, their exclusionary effect, even if not simply a reflection of one party's cost structure and therefore of competition on the merits, "is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting." *Brooke Group*, 509 U.S. at 223. As the Court explained, a looser standard would run the risk of imposing liability in cases involving procompetitive price-cutting, and "the costs of [such] an erroneous finding of liability are high," *id.* at 226, because such errors (or "false positives") would "chill the very conduct the antitrust laws are designed to protect," *ibid.* (internal quotation marks and citation omitted). The risk that such "false positives" will occur under a looser standard is substantial, the Court explained, because "[t]he mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition." *Ibid.* (internal quotation marks and citation omitted) (brackets in original); see *Barry Wright Corp.* v. *ITT Grinnell Corp.*, 724 F.2d 227, 231 (1st Cir. 1983) (Breyer, J.) (observing that "a legal precedent or rule of law that prevents a firm from unilaterally cutting its prices risks interference with one of the Sherman Act's most basic objectives: the low price levels that one would find in well-functioning competitive markets").

It is also true that a margin-based price squeeze could in theory inflict anticompetitive harms. In *Town of Concord*, the First Circuit discussed two potential harms it viewed as "the most important of those that favor prohibiting a price squeeze," although it recognized that scholars disputed their "practical significance." 915 F.2d at 24. First, extending the upstream monopoly to the downstream level could

"raise[] 'entry barriers,' thereby fortifying [the upstream] monopoly position." *Id.* at 23. Absent formidable preexisting entry barriers upstream, however, there would be no upstream monopoly. Thus, as a leading treatise concludes, "[e]ven when a monopolist at one essential stage 'monopolizes' a second stage, consumer harm cannot be inferred and is difficult to identify. * * * [W]e think competitive injury is the exception rather than the rule." 3A *Antitrust Law* ¶ 756b at 11; see *id.* ¶ 756c3 at 20 ("adverse effects are far from certain").

Second, preserving downstream competitors can provide *non-price* competition that may result in consumer benefits. *Town of Concord*, 915 F.2d at 24. But interfering with pricing in the marketplace in order to preserve the benefits of non-price competition is not sound antitrust policy, particularly because the second-level firms may not be especially innovative. Although the *Town of Concord* court was "willing to assume" those two potential harms would justify prohibiting price squeezes "were there nothing to be said in favor of permitting prices that could create such a squeeze," *ibid.*, it recognized that there are strong reasons to permit such prices. Likewise, on balance there is no sufficiently sound foundation for prohibiting price squeezes based solely on the margin between a vertically-integrated defendant's wholesale and retail prices.[17]

That conclusion holds true whether the relevant market is regulated, partially regulated, or unregulated. In *Town of Concord*, while declining to apply *Alcoa* to a fully regulated industry, 915 F.2d at 28, the First Circuit observed "that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregu-

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[17] In reaching a contrary conclusion, see Resp. Supp. Cert. Br. 1a-14a, the FTC relied primarily on the Second Circuit's outmoded decision in *Alcoa* and failed to take sufficient account of *Trinko*, *Brooke Group*, and this Court's other recent antitrust jurisprudence.

lated level, in order to earn at that second level the very profits that regulation forbids at the first," *id.* at 29. But that is essentially a problem of regulatory evasion, not of antitrust law. Cf. *NYNEX Corp.* v. *Discon, Inc.*, 525 U.S. 128, 135-137 (1998) (emphasizing importance of showing harm to "competitive process" and distinguishing "the exercise of market power that is *lawfully* in the hands of a monopolist" even if combined with regulatory evasion). Moreover, even though the FCC regulates only petitioners' wholesale rates, it can consider price-squeeze allegations as a matter of regulatory law in assessing those rates. See, *e.g.*, *FPC* v. *Conway Corp.*, 426 U.S. 271 (1976) (holding that the FPC can consider allegations of price squeeze by regulated firm even though retail rates were not within its jurisdiction); *Sprint Commc'ns Co.* v. *FCC*, 274 F.3d 549 (D.C. Cir. 2001) (holding that FCC can consider price squeeze allegations in public interest determination although retail rates are not within its jurisdiction). In any event, if, as suggested above, there is no sound basis to treat margin-based price squeezes as antitrust violations even in unregulated markets, there is surely no reason to do so in wholly or partially regulated markets.

4. Like the Second Circuit's theory in *Alcoa*, the price-squeeze theory reaffirmed by the Ninth Circuit forbids pricing wholesale inputs so high that the defendant's "customers cannot compete with it in the second-level" market. Pet. App. 8a (internal quotation marks omitted). Under that reasoning, what makes the conduct purportedly unlawful is its adverse effect on a competitor. See J.A. 17 (¶ 19) (alleging that petitioners' price squeeze placed respondents at a "serious unfair disadvantage"). But, for all the reasons explained above, a complaint in which the allegations of anticompetitive conduct are limited to such a squeeze does not suffice to establish that "the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2); see *Bell Atl. Corp.* v. *Twombly*,

127 S. Ct. 1955, 1965 (2007) (noting that a complaint's "[f]actual allegations must be enough to raise a right to relief above the speculative level"). The court of appeals was therefore wrong to conclude that respondents' price-squeeze allegations stated a valid antitrust claim.[18]

Accordingly, respondents' price-squeeze theory could not sufficiently state a claim without additional allegations of anticompetitive conduct. Allegations satisfying the *Brooke Group* requirements with respect to the retail market might suffice. But then the gravamen of the complaint would no longer be a price squeeze (*i.e.*, an insufficient margin between wholesale and retail prices) as such, but rather the predatory nature of petitioners' retail price. As the dissent concluded (Pet. App. 20a-21a), for such a complaint to be viable, it would have to satisfy *Brooke Group* by alleging that "the prices complained of are below an appropriate measure of its rival's costs" and that the defendant had "a dangerous probability[] of recouping its investment in below-cost prices." 509 U.S. at 222, 224.

The panel majority adverted to the possibility that respondents "could prove facts, consistent with [their] complaint, that involve only unregulated behavior at the retail level." Pet. App. 18a. But unlike the dissenting judge, the majority did not hold or suggest that a price-squeeze complaint must contain allegations sufficient to satisfy the *Brooke Group* standard in order to survive a motion for judgment on the pleadings. *Id.* at 19a. The Ninth Circuit's reaffirmation (*id.* at 14a) of "price squeeze theory" as a

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[18] In contrast, two other circuits have correctly recognized that *Trinko* and *Brooke Group* combine to bar a margin-based price-squeeze claim. See *Covad Commc'ns Co.* v. *BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004), cert. denied, 544 U.S. 904 (2005); *Covad Commc'ns Co.* v. *Bell Atl. Corp.*, 398 F.3d 666, 673 674 (D.C. Cir.), order on denial of reh'g, 407 F.3d 1220, 1222 (D.C. Cir. 2005); see also U.S. Invitation Br. 15-16.

"viable" and independent "part of the fabric of traditional antitrust law" cannot be squared with this Court's modern antitrust cases.

CONCLUSION

The judgment below should be vacated and the case remanded for further proceedings.

Respectfully submitted.

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AMICUS CURIAE BRIEF

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In the Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
DBA AT&T CALIFORNIA, ET AL., PETITIONERS

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
RESPONDENTS

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR ABBOTT LABORATORIES AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether a plaintiff states a claim under Section 2 of the Sherman Act, 15 U.S.C. § 2, by alleging that the defendant—a vertically integrated retail competitor with an alleged monopoly at the wholesale level—engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete, when the defendant has no antitrust duty to provide the wholesale input to the plaintiff.

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INTRODUCTION AND INTEREST OF *AMICUS CURIAE*

Under the Ninth Circuit's decision in this case, any vertically integrated company that has a lawful monopoly at the wholesale level is potentially subject to "price squeeze" liability regardless of whether the plaintiff alleges—or can prove—that the company has engaged in predatory pricing at the retail level. As this Court has recognized, however, firms have every right to charge high prices for products on which they hold a lawful monopoly; that right is what creates the incentive for a great deal of beneficial innovation. Moreover, this Court's precedents establish that "low" prices do not violate the antitrust laws unless they are set below a firm's costs with a realistic prospect that the firm will later be able to recoup its losses.[1]

In short, absent a claim of below-cost pricing that meets the stringent standards of *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), the combination of a legitimate monopolist's high wholesale prices and its low but above-cost retail prices simply does not add up to a viable antitrust claim under Section 2 of the Sherman Act.

In so holding, moreover, it is important that the Court make clear that liability for unilateral pricing decisions should be limited to situations in which a firm sets prices below its incremental costs (meas-

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[1] No counsel for a party authored this brief in whole or in part, and no person or entity other than the *amicus* or its counsel made a monetary contribution to the preparation or submission of the brief. Pursuant to Rule 37.3(a), petitioners filed with the Court a blanket consent for all *amici*, and respondents separately consented to the filing of this brief. Confirmation of respondents' consent is on file with the Clerk.

ured by average variable costs) and there is a dangerous probability that it will recoup its losses after competitors are driven from the market. Any other rule would put courts in the position of a price-control board and would discourage companies from innovating and competing fairly on the basis of low prices—all to the detriment of consumers.

Amicus Abbott Laboratories, a global health care company devoted to discovering new medicines and life-saving technologies, has a vital interest in the resolution of the issue presented here. Many of Abbott's products, which span the continuum of health care from nutritional products and laboratory diagnostics to medical devices and pharmaceutical therapies, are covered by one or more patents that confer upon Abbott a lawful monopoly over the patented product. Moreover, because it operates in every United States jurisdiction, Abbott has a strong interest in ensuring that the antitrust laws are applied uniformly, and that its pricing decisions are not subject to varying standards in different jurisdictions.

STATEMENT

This antitrust action involves the right of a company to unilaterally set its prices in the absence of an antitrust duty to deal with its customers. Respondents (collectively "linkLine") are Internet Service Providers (ISPs) that lease access for Digital Subscriber Lines (DSL) from petitioners Pacific Bell Telephone Company, et al. (collectively "AT&T"). linkLine alleges that AT&T charged too "high" a price for that access relative to the price that it charged for retail DSL Internet-access services, thereby creating a "price squeeze" in violation of § 2 of the Sherman Act.

AT&T argued below that this Court's decision in *Verizon Communications, Inc.* v. *Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), disposed of linkLine's claim because AT&T had no antitrust duty to deal with linkLine, much less a duty to offer it a favorable price for access. A divided panel of the Ninth Circuit disagreed, holding that while the prices charged by AT&T to ISPs at the wholesale level were regulated by federal telecommunications laws, "linkLine could prove facts * * * that involve only unregulated behavior at the retail level." *linkLine Communs., Inc.* v. *Pacific Bell Tel. Co.*, 503 F.3d 876, 885 (9th Cir. 2007). Because of the possibility that AT&T's price for its retail services was sufficiently low to cause a "price squeeze," the panel's majority reasoned that the claim could survive a motion for judgment on the pleadings. *Ibid.*

Judge Gould dissented, explaining that "*Trinko* insulates from antitrust review the setting of the upstream price." *Id.* at 886-887 (Gould, J. dissenting). In other words, because *Trinko* permitted AT&T to refuse to deal with linkLine altogether, *a fortiori* AT&T was free to charge a monopoly price in the upstream market for wholesale DSL access. *Ibid.* As a result, all that remained of the claim was the challenge to AT&T's unilateral pricing decision at the retail end. *Id.* at 885-886. And since linkLine failed to allege that AT&T's prices "were below cost, under any measure of cost"—an essential element of a predatory pricing claim under *Brooke Group*—Judge Gould explained that "the case doesn't get out of the antitrust law starting blocks." *Id.* at 885-886.

SUMMARY OF ARGUMENT

Under this Court's precedents, as well as economic common sense, Judge Gould was right.

I. The antitrust laws do not restrict the ability of a vertically integrated company with a monopoly in the upstream market to set "high" monopolistic prices at the wholesale level. Under the allegations here, petitioners have lawful monopoly power as regulated participants in the upstream market for DSL transport (high-speed digital subscriber line service). And this Court's decision in *Trinko*—which confirms that AT&T had no antitrust duty to deal with respondents at all—logically means that the antitrust laws do not preclude AT&T from setting wholesale prices at a level that effectively accomplishes the same result.

In many industries, moreover, the ability to set monopolistic prices provides an essential incentive for needed innovation—which is critical to the health of any market economy and, hence, to consumer welfare. If affirmed, the Ninth Circuit's rule would directly undermine that incentive.

Given the right of vertically integrated firms to set "high" wholesale prices for products on which they hold a lawful monopoly, the antitrust laws impose no liability for a "price squeeze" absent a showing of anticompetitive pricing in the downstream, retail market. Under a long line of this Court's decisions, that means the defendant must have set its prices at a level below its costs and must have been likely to recoup its losses after driving its competitors from the market. But respondents here have failed to allege even below-cost pricing, let alone a substantial probability of recoupment.

Moreover, if the Court were to craft an exception to its below-cost rule for "price squeeze" cases, consumers would suffer. In an effort to avoid the risk of antitrust liability for aggressive but above-cost pricing, efficient firms would err on the side of higher prices, thereby harming consumers directly. And inefficient firms—including firms that ought to exit the market—would be protected by the conservative pricing decisions of their more efficient rivals. The Ninth Circuit's rule is thus fundamentally inconsistent with the purpose of antitrust law, which is to foster competition, not to force more efficient firms to set prices at an artificially high level, thus keeping their less efficient competitors afloat and, in the process, hurting consumers.

II. Under sound economic theory and this Court's precedent, unilateral pricing should not be considered "predatory" absent a showing that it is below the incremental (or average variable) cost of producing the product at issue. The only unilateral pricing strategy that can harm consumers in the long run is one that makes it impossible for equally efficient rivals to cover their variable costs. As economists across the spectrum have recognized, that level is average variable costs, not total costs, because firms generally do not exit a market if they are at least breaking even on each new sale.

Moreover, a uniform rule—no pricing below average variable costs during the allegedly predatory period—would not only give firms the certainty they need to make pricing decisions that benefit consumers, but it would also save courts from having to second-guess those decisions.

ARGUMENT

I. Vertically integrated firms with lawful monopoly power in the upstream market should not be held liable for unilateral pricing activity unless they engaged in below-cost pricing at the retail level.

As the dissent below recognized, this case is nothing more than an improperly pled predatory pricing case. 503 F.3d at 885 (Gould, J., dissenting). Although respondents allege that petitioners engaged in a "price squeeze" by setting "high" wholesale prices and "low" retail prices, they have failed to state a claim on either end. As demonstrated below in Part I.A., this Court's precedents, including most recently *Trinko*, establish that the antitrust laws permit any vertically integrated company with lawful monopoly power in the upstream market to set *wholesale* prices as it chooses—subject only to the law of supply and demand. And once the legality of petitioners' wholesale pricing activity is established, respondents cannot hope to make out a predatory pricing claim on the *retail* end. As shown in Part I.B., under several of this Court's precedents, firms cannot be held liable for unilateral pricing activity unless they priced their goods below an appropriate measure of their costs and there was a substantial probability that they would recoup their losses—neither of which has been alleged in this litigation.

A. The antitrust laws permit lawful monopolists to charge monopoly prices.

We begin with a fundamental but often overlooked principle: Plaintiffs alleging a violation of Section 2 of the Sherman Act must establish not only that the defendant possesses monopoly power, but also "the

willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States* v. *Grinnell Corp.*, 384 U.S. 563, 570-571 (1966). Legitimate monopolists, in other words, may reap the fruits of their monopolies without violating the antitrust laws, so long as they do not stray into "anticompetitive *conduct*." *Trinko*, 540 U.S. at 407.

On the wholesale side of the ledger, the only "anticompetitive" conduct that respondents allege is "high" prices. But the idea that *courts* should determine when a price becomes "unreasonable" has long been foreclosed by this Court's decisions. *United States* v. *Trenton Potteries Co.*, 273 U.S. 392, 397-398 (1927).

Moreover, it is well settled that the ability to set high prices is a legitimate fruit of a legal monopoly. As this Court explained in *Trinko*, the "charging of monopoly prices[] is not only not unlawful; it is an important element of the free-market system." 540 U.S. at 407. As a matter of basic economic theory, "[t]he opportunity to charge monopoly prices—at least for a short period—is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth." *Ibid.*

Accordingly, in order "[t]o safeguard the incentive to innovate," courts should not interfere with the reaping of monopoly profits "unless it is accompanied by an element of anticompetitive conduct." *Ibid.*; see also *id.* at 407-408 ("Compelling [monopolies] to share the source of their advantage * * * may lessen the incentive for the monopolist, the rival, or both to invest in * * * economically beneficial facilities."). And as the D.C. Circuit has observed, setting "an excessive

price alone does not establish a violation of the antitrust laws, because imposition of a high price is not, in and of itself, an anticompetitive act." *Williamsburg Wax Museum, Inc.* v. *Historic Figures, Inc.*, 810 F.2d 243, 252 (D.C. Cir. 1987).

This case involves the alleged abuse of monopoly power in the arena of telecommunications, a regulated industry. But the law allows (and sometimes encourages) monopolies in other contexts as well, whether because of natural economies of scale or because the government views monopoly status as an effective means of encouraging innovation.

Indeed, the Constitution itself sanctions granting monopolies for that purpose: To "promote the Progress of Science and useful Arts," patents give "Inventors the exclusive Right to their respective * * * Discoveries." U.S. CONST. art. I § 8. Only when patent holders use their patents to engage in anticompetitive activity do they become subject to the antitrust laws, *United States* v. *Singer Mfg. Co.*, 374 U.S. 174, 197 (1963), and the charging of monopoly prices does not amount to anticompetitive activity. Naturally, the market itself imposes limits on a patent holder's ability to dictate the price of its product; the fact that there is no perfect substitute for a patented product does not mean that demand for that product is entirely inelastic—*i.e.*, that a firm may ignore the effect of its price on sales. Richard A. Posner, *Antitrust Law* 64 (2d ed. 2001). That said, "[a] patent empowers the owner to exact royalties as high as he can negotiate with the leverage of that monopoly." *Brulotte* v. *Thys Co.*, 379 U.S. 29, 33 (1964).

This Court's precedents thus confirm that whether a vertically integrated company has lawful monopoly

power in the upstream market by virtue of "growth or development as a consequence of a superior product, business acumen, or historic accident," *Trinko*, 540 U.S. at 407 (citation omitted), the antitrust laws do not restrict its ability to charge monopoly prices at the wholesale level. Moreover, just as those laws permit a legitimate monopolist to altogether refuse to deal with its competitors, such a monopolist may lawfully accomplish the same result by setting prices at a level that its competitors find unreasonable. *Trinko*, 540 U.S. at 409; see also *Covad Communs. Co.* v. *Bell Atl. Corp.*, 398 F.3d 666, 673 (D.C. Cir. 2005).

B. This Court has consistently foreclosed liability under the antitrust laws for above-cost pricing.

Because respondents failed to state a claim at the wholesale level under *Trinko*, their claim boils down to a challenge to petitioners' unilateral pricing activity at the retail level. One searches the complaint in vain, however, for an allegation of below-cost pricing. The Ninth Circuit's decision should therefore be recognized for what it is—the imposition of a rule that forces vertically integrated firms to set retail prices based on concern, not for consumers, but for rivals.

Any such rule would be highly suspect, inasmuch as "[l]ow prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition." *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U.S. 328, 340 (1990). Indeed, each time this Court has addressed the standards for allegedly anticompetitive pricing, it has held that plaintiffs must allege and prove below-cost pricing. See, *e.g.*, *Matsushita Elec. Indus. Co.* v. *Zenith Radio Corp.*, 475 U.S. 574 (1986);

Cargill, Inc. v. *Monfort of Colo., Inc.*, 479 U.S. 104 (1986); *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U.S. 328 (1990); *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993); *Weyerhaeuser Co.* v. *Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069 (2007). As noted in *Atlantic Richfield Co.*, moreover, the Court "ha[s] adhered to this [below-cost] principle *regardless of the type of antitrust claim involved.*" 495 U.S. at 340 (emphasis added).

1. The Court has consistently declined to recognize an exception to the rule that unilateral pricing activity is lawful unless set at below-cost rates.

A few examples illustrate the Court's consistent rejection of any exceptions to this below-cost rule. In *Matsushita*, American electronics companies alleged that their Japanese counterparts, in an effort to drive their American competitors out of business, conspired to sell electronics at predatory prices. 475 U.S. at 584. Once they succeeded, the American companies alleged, the Japanese companies would restrict output and raise prices to a supracompetitive level, thereby recouping "the losses they incurred through years of pricing below market level." *Ibid.*

Holding that the plaintiffs' theory of liability was legally insufficient to withstand summary judgment, this Court confirmed that predatory pricing "means pricing *below* some appropriate measure of cost." *Id.* at 585 n.8 (emphasis added). Selling above these levels, moreover, "would either leave [competitors] in the same position as would market forces or would actually benefit [them] by raising market prices." *Ibid.*

Accordingly, above-cost pricing could not possibly be predatory.

Cargill is to the same effect. There the plaintiff sought to enjoin rival meat-packing firms from merging and thereafter engaging in a "price-cost squeeze" whereby they would bid up the price of cattle while reducing the price of beef sold to consumers. 479 U.S. at 107-108. At the retail level, however, the plaintiff alleged only that the merged company would lower its prices to a level "at or slightly above its costs." *Id.* at 114. As a result, this Court rejected the plaintiff's claim, stating: "To hold that the antitrust laws protect competitors from the loss of profits due to such price competition would, in effect, render illegal any decision by a firm to cut prices in order to increase market share." *Id.* at 116. Antitrust liability for predatory pricing requires a showing of "pricing below an appropriate measure of cost for the purpose of eliminating competitors in the short run and reducing competition in the long run." *Id.* at 117 & n.12.

Similarly, *Brooke Group* involved allegations that the defendant sold generic cigarettes at a predatory price in an effort to drive its rivals from the market, in alleged violation of the Robinson-Patman Act. 509 U.S. at 212. This Court ruled for the defendants as a matter of law, holding that plaintiffs had failed to "prove that the prices complained of are below an appropriate measure of its rival's costs" and to prove "a reasonable prospect [under Robinson-Patman], or, under § 2 of the Sherman Act, a dangerous probability, of [the defendant] recouping its investment in below-cost prices." *Id.* at 222, 224. As the Court noted, "the reasoning in both [the *Matsushita* and *Cargill*] opinions suggests that only below-cost prices should suffice, and we have rejected elsewhere the notion

that above-cost prices that are below general market levels or the costs of a firm's competitors inflict injury to competition cognizable under the antitrust laws." *Id.* at 223.

The Court acknowledged that the requirements it set forth "are not easy to establish," but that did not deter it from holding that they "are essential components of real market injury." *Id.* at 226. That is because "[t]he mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition." *Ibid.* Thus, "the costs of an erroneous finding of liability are high," and include "chill[ing] the very conduct the antitrust laws are designed to protect." *Ibid* (internal quotations omitted).

The Court in *Brooke Group* acknowledged, moreover, that "[a]s a general rule," low but above-cost pricing "either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting." *Id.* at 223. Thus, as the Court recognized, both sound economic theory and the courts' institutional limitations warrant interpreting the antitrust laws to restrict unilateral pricing activity *only* if it is below a firm's costs.

Just two Terms ago, the Court unanimously reaffirmed and extended the holding of *Brooke Group* in forceful terms. In *Weyerhaeuser*, the Court held that the *Brooke Group* test applied not only to predatory pricing, but also to predatory bidding, in which firms bid up the prices of inputs in an effort to drive rivals from the market. 127 S. Ct. at 1072, 1075. As the Court explained, satisfying the two prongs of the

Brooke Group test are "prerequisites to recovery." *Id.* at 1074. Thus, "only higher bidding that leads to below-cost pricing in the relevant output market will suffice as a basis for liability for predatory bidding." *Id.* at 1078. The Court left no room for any claim of predatory bidding absent a showing that the defendant sold goods at below-cost prices.

As the foregoing body of precedent confirms, this Court has been unwavering in its insistence that unilateral pricing activity cannot be predatory unless the defendant firm reduces its prices below its costs. The Court has not recognized any exception to this rule, despite having addressed the question under several statutes and in varied factual contexts. Rather, this Court "ha[s] adhered to this [below-cost] principle regardless of the type of antitrust claim involved." *Atlantic Richfield Co.*, 495 U.S. at 340. Respondents' failure to allege below-cost pricing is therefore fatal to their "price squeeze" claim.[2]

[2] Notwithstanding the substantial precedent discussed in the text, certain lower courts have interpreted the below-cost rule as limited in scope. *E.g.*, *LePage's, Inc.* v. *3M*, 324 F.3d 141, 151 (3d Cir. 2003) (en banc) (declining to apply *Brooke Group* to a bundled discount claim); *Meijer, Inc.* v. *Abbott Labs.*, 544 F. Supp. 2d 995, 1003 (N.D. Cal. 2008) (holding that an above-cost unilateral pricing decision in the pharmaceutical industry "is a strong candidate for the exception" to the below-cost rule). See also Antitrust Modernization Comm'n, Report and Recommendations 10, 94 (2007) (criticizing *LePage's* on the ground that it "offers no clear standards by which firms can assess whether their bundled rebates are likely to pass antitrust muster").

2. The Court's refusal to extend antitrust liability to above-cost pricing is consistent with the fundamental purpose of the antitrust laws—protecting consumers.

As the foregoing authorities indicate, antitrust liability for above-cost pricing conflicts with the major goal of antitrust law—fostering competition that benefits consumers. See Herbert Hovenkamp, *Federal Antitrust Policy* § 1.1 (1994) ("An important goal of antitrust law—arguably its only goal—is to ensure that markets are competitive."); Robert H. Bork, *The Antitrust Paradox* 51 (2d ed. 1993) ("The only legitimate goal of American antitrust law is the maximization of consumer welfare."). Indeed, as this Court has repeatedly recognized, "cutting prices in order to increase business often is the very essence of competition." *Matsushita*, 475 U.S. at 594. "It would be ironic indeed if the standards for predatory pricing liability were so low that antitrust suits themselves became a tool for keeping prices high." *Brooke Group*, 509 U.S. at 226-227. Without a clear safe harbor for above-cost price cutting, firms will be reluctant to make unilateral pricing decisions that pass on lower costs to customers. They will instead be compelled to err on the side of higher prices. *Ibid.*

Any exception to the below-cost rule would harm consumers in at least two ways. First, they would pay higher prices for goods in the short term because the exception would likely make firms fearful of antitrust liability if they engaged in aggressive but above-cost pricing. Such a result would be in direct tension with this Court's oft-repeated observation that "[l]ow prices benefit consumers regardless of how those prices are set, and so long as they are above preda-

tory levels, they do not threaten competition." *Atlantic Richfield Co.*, 495 U.S. at 340.

Second, less efficient firms would be protected by conservative pricing decisions from their more efficient rivals. As a result, those firms would have less incentive to become more efficient and to pass on those savings to consumers. Herbert Hovenkamp, *supra*, § 8.1. And that would tend to keep prices inflated in the long term. *Ibid.*

These harms, moreover, could well occur even in markets where an antitrust claim is unlikely to succeed for other reasons. For example, even if a below-cost predatory pricing scheme could not possibly work in a given market because of the relative ease of entry (or reentry)—providing a solid defense to potential antitrust defendants—firms may still be deterred from aggressive above-cost price-cutting because of the legal uncertainty created by an exception to the above-cost pricing safe harbor. See Einer Elhauge, *Why Above-Cost Price Cuts To Drive Out Entrants Are Not Predatory*, 112 Yale L.J. 681, 686-687 (2003).

Such legal uncertainty is no trivial matter given the ubiquity of discounts for "bundled" products in today's economy. Bundled discounts are used, for example, by airlines selling multi-stop flights and a host of other companies offering "one-stop" shopping rather than isolated components. *Id.* at 735.

Firms making any of these unilateral but consumer-friendly pricing decisions need certainty, lest they risk running afoul of a lower court that purports to find an exception to the below-cost rule set forth in *Brooke Group*. Moreover, should *this* Court create such an exception, many weaker firms would simply launch antitrust suits rather than try to match the

aggressive prices of their rivals. Although actual predatory pricing is rare, "competitors allege predation frequently." Phillip Areeda & Herbert Hovenkamp, 3 *Antitrust Law* § 723a (2d. ed. 2002). Moreover, "[u]nhappy rivals may automatically assume predation when a competitor's price is below their own costs, disregarding the possibility that the alleged predator's cost is well below theirs and more than covered by its price." *Ibid.* As the Antitrust Modernization Commission recently explained, a "lack of clear standards" may therefore "discourage conduct that is procompetitive or competitively neutral and thus may actually harm consumer welfare." Antitrust Modernization Comm'n, Report and Recommendations 12 (2007).

Indeed, allowing antitrust liability for unilateral above-cost pricing might encourage inefficient firms to enter or remain in the market in hopes of taking advantage of the higher prices. Cf. Hovenkamp, *supra*, § 8.1 (The result of using "an overdeterrent rule * * * will be inefficient high prices. This in turn will permit less efficient firms to stay in the market."). But the purpose of antitrust law is not to coddle weaker firms, or to force more efficient firms to lend a helping hand to less efficient competitors by establishing "reasonable" prices that keep them afloat. Such perverse incentives "will mean higher costs and lower product quality for society generally." Elhauge, *supra*, 112 Yale L.J. at 688.

Predatory pricing standards should therefore err on the side of underinclusiveness, avoiding what this Court has called the "cost of false positives." *Trinko*, 540 U.S. at 414. It is true that an underinclusive rule might theoretically allow marginally predatory behavior to go unpunished. But "[i]ll-conceived or ill-

defined rules impose heavy social costs by deterring legitimate pricing and by both increasing and complicating litigation." Areeda & Hovenkamp, *supra*, § 723b. Accordingly, "the best course is to develop predation rules that are somewhat underdeterrent, with the benefit of any doubt generally given to the defendant." *Ibid.* As Judge Robert Bork has put it, any attempt to enforce strict rules against predatory pricing "would do much more harm than good." Bork, *supra*, at 154.

In sum, a clear below-cost rule for unilateral pricing liability achieves the balance of deterring truly predatory behavior while encouraging aggressive pricing that benefits consumers in a wide range of contexts. This Court should therefore reaffirm "that only below-cost prices should suffice" to support antitrust liability for unilateral pricing decisions. *Brooke Group*, 509 U.S. at 223.

II. Prices should not be considered predatory unless they fall below incremental cost, as measured by average variable costs.

The remaining question is how "cost" should be determined. Although this Court has strongly suggested that a plaintiff should not be able to recover for predatory pricing "when the pricing in question is above some measure of *incremental* cost," it has not authoritatively resolved the issue of what measure of "cost" should serve as the baseline for *Brooke Group*'s rule. See *Brooke Group*, 509 U.S. at 223 (emphasis added) (citing *Cargill*, 479 U.S. at 117-118 n.12 (quoting *Matsushita*, 475 U.S. at 585 n.9)). As a result, the lower courts now set their own, sometimes conflicting, standards, thereby deterring legitimate price-cutting behavior and creating uncertainty for firms

that market products in multiple regions.[3] We therefore urge the Court to confirm that a firm's prices are predatory only if they are set below the firm's *incremental* costs, or its close surrogate, average variable costs.[4] This approach is consistent not only with this Court's guidance, but with economic theory and the fundamental purposes of antitrust.

1. As noted above, the fundamental goal of antitrust is to foster competition for the benefit of con-

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[3] See, *e.g.*, *Northeastern Tel. Co.* v. *AT&T*, 651 F.2d 76, 88 (2d Cir.1981) (average variable cost); *Cascade Health Solutions* v. *Peacehealth*, 515 F.3d 883, 906 (9th Cir. 2008) (incremental cost); *Instructional Sys. Dev. Corp.* v. *Aetna Cas.*, 817 F.2d 639, 648 (10th Cir. 1987) (prices above average variable costs may be predatory in the presence of factors such as a price increase once a competitor leaves the market or a decrease when a competitor enters); *Spirit Airlines, Inc.* v. *Northwest Airlines, Inc.*, 431 F.3d 917, 938 (6th Cir. 2005) (adopting a burden-shifting approach under which the court finds a prima facie case of predation when costs fall below average variable costs, but the plaintiff bears the burden of proving predation when costs are above average variable costs but below average total costs); *Barry Wright Corp.* v. *ITT Grinnell Corp.*, 724 F.2d 227, 233-236 (1st Cir. 1983) (same); *Henry* v. *Chloride, Inc.*, 809 F.2d 1334, 1346 (8th Cir. 1987) (same); *McGahee* v. *Northern Propane Gas*, 858 F.2d 1487, 1496 (11th Cir. 1988) (same); see also *Brooke Group*, 509 U.S. at 223 n.1 ("Because the parties in this case agree that the relevant measure of cost is average variable cost, * * * we again decline to resolve the conflict among the lower courts over the appropriate measure of cost.").

[4] Incremental (or marginal) cost measures how much firms spend to produce each additional unit of goods or services. Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 Harv. L. Rev 697, 700 (1975). Because incremental cost is often difficult to measure, however, average variable cost is often used in its stead. *Id.* at 716-717. By contrast, average total cost is the total cost—both fixed and variable—of producing goods and services, divided by the total units produced. *Id.* at 700-701.

sumers. See Hovenkamp, *supra*, § 1.1; Bork, *supra*, at 51. The law does so *not* by ensuring that all firms survive regardless of their relative strengths and weaknesses. Rather, it does so by ensuring that firms do not gain or use monopoly power in a way that is detrimental to consumers. *Grinnell*, 384 U.S. at 570-71; *Cargill*, 479 U.S. at 118 ("In contrast to price cutting aimed simply at increasing market share, predatory pricing has as its aim the elimination of competition.").

That is why, insofar as unilateral price reductions are concerned, the concern of antitrust law has always been limited to the possibility that one firm might drive an equally or more efficient competitor from the market, and do so permanently. In general, price reductions are good for consumers, even if they force less efficient firms to leave the market. As Judge Posner has observed, "[a] seller may want to destroy a competitor, but if the only method used is underselling him by virtue of having lower costs there is no rational antitrust objection to the seller's conduct." Posner, *supra*, 214.

The only way a unilateral price reduction can harm *consumers* is if it forces equally or more efficient firms to exit the market permanently. But firms will not be forced to exit a market if they are breaking even on each additional or incremental unit of the product or service they sell—that is, if they are covering their variable costs. Areeda & Turner, *supra*, at 701-702. Even if they are not recouping fixed costs, which are already sunk, firms will likely not abandon the effort unless they are losing money on each new sale. Bork, *supra*, at 150. And they will only be losing money on each new sale if the price they charge is less than their variable costs.

Firms that are breaking even on each new sale are particularly unlikely to abandon the market when the period of low pricing is likely to be relatively short, as it is with predatory or aggressive pricing before the firms involved again seek more robust profits. Efficient firms can weather the storm of aggressive pricing without losing money, then return to profitability once the storm passes.

Of course, incremental or variable costs cannot ordinarily be measured directly. And that is why economists typically use *average* variable costs—a well-established accounting measure—as a proxy for variable costs. See Areeda & Turner, *supra*, at 716-718.

For all these reasons, the average variable cost test is widely accepted among economists and antitrust scholars as the most appropriate judicial test for determining the propriety of unilateral pricing reductions. A unilaterally determined price must be below that level before it can create any serious risk that an equally efficient firm will exit the market, thus harming consumers.[5]

2. Adopting this uniform standard—average variable costs—will not only give firms the certainty they need to make pricing decisions that benefit consumers, it will also remove courts from the difficult posi-

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[5] *E.g.*, Areeda & Turner, *supra*, at 702 (arguing that although short-run marginal cost is the better measure, average variable cost is a more usable surrogate); Areeda & Hovenkamp, *supra*, § 724c; Janusz A. Ordover & Robert D. Willig, *An Economic Definition of Predation*, 91 Yale L.J. 8, 17 (1981); Bork, *supra*, at 150; William J. Baumol, *Predation and the Logic of the Average Variable Cost Test*, 39 J.L. & Econ. 49, 57 n.13, 58-59 (1996) (proposing a variation called "average avoidable costs" as the cost standard); Elhauge, *supra*, 112 Yale L.J. at 707-708.

tion of second-guessing those decisions. Courts need a clear benchmark such as average variable cost to make reliable and predictable decisions. Conversely, allowing courts to retain significant flexibility in determining what pricing standards to apply (and when to apply them) serves neither the courts nor the parties well. *Northeastern Tel. Co.* v. *AT&T*, 651 F.2d 76, 88 (2d Cir. 1981) ("[W]hen the costs of a misjudgment are high and the prevalence of the conduct the law seeks to deter is low, simpler rules are preferable.").

That is true, in part, because antitrust claims involving unilateral pricing decisions are particularly difficult for courts to resolve with any confidence. See Posner, *supra*, at 214 (discussing the "difficulty of distinguishing between predatory and efficient pricing"). As Judge Bork has observed of price regulation by courts and enforcement agencies, "[t]here is a high probability of mistake, and hence of harassment, by enforcement authorities and private plaintiffs that would harm consumers by inducing noncompetitive price behavior." Bork, *supra*, at 154.

Accordingly, because antitrust law is designed to encourage competition that leads to low prices, courts should give firms significant leeway in crafting aggressive pricing strategies. "If the judge uses an overdeterrent rule the result will be inefficiently high prices." *Ibid.*

Judge Easterbrook has expressed related concerns about over-deterrent antitrust rules: "If the court errs by condemning a beneficial practice, the benefits may be lost for good. Any other firm that uses the condemned practice faces sanctions in the name of stare decisis, no matter the benefits." Frank H.

Easterbrook, *The Limits of Antitrust*, 63 Texas L. Rev. 1, 2-3 (1984). An under-deterrent rule, by contrast, will likely be corrected by the market: "If the court errs by *permitting* a deleterious practice the welfare loss decreases over time" because the resulting monopoly prices will eventually attract new entrants, thereby increasing competition and reducing prices to consumers. *Ibid.* (emphasis added).

Furthermore, actual predatory pricing is particularly difficult to accomplish, and thus is rare. Areeda & Turner, *supra*, at 699. As a result, courts that over-enforce rules against predatory pricing will almost inevitably punish innocent, pro-competitive behavior, whereas courts that under-enforce those rules have some assurance that, in the end, the market will correct their errors.

The difficulty that judges face in determining whether a firm's prices violate the antitrust laws was highlighted by then-Judge Breyer in *Town of Concord* v. *Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990):

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap"? Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does

> one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will?

Id. at 25. Given the difficulty of these questions, it is not surprising that then-Judge Breyer would see in the judicial administration of pricing rules "a significant risk that a court's efforts to stop such price requests will bring about the very harms—diminished efficiency, higher prices—that the antitrust laws seek to prevent." *Id.* at 19. That is "why antitrust courts normally avoid direct price administration, relying on rules and remedies (such as structural remedies, *e.g.*, prohibiting certain vertical mergers) that are easier to administer." *Id.* at 25.

This Court has itself recently recognized the difficulties of administering finely tuned pricing rules. As the Court observed in *Trinko*, "[e]ven if the problem of false positives did not exist, conduct consisting of anticompetitive violations * * * may be, as we have concluded with respect to above-cost predatory pricing schemes, beyond the practical ability of a judicial tribunal to control." 540 U.S. at 414 (internal quotations omitted). The Court there explained that when "antitrust courts * * * act as central planners, identifying the proper price, quantity, and other terms of dealing," they fulfill "a role for which they are ill suited." *Id.* at 408.

This case gives the Court an opportunity to ease these difficulties by adopting what Judge Easterbrook has called a "simple presumption"—a presumption that will "mak[e] it possible for counsel to state that some things do not create risks of liability," and thereby "reduce the costs of litigation by designating

as dispositive particular topics capable of resolution." Easterbrook, *supra*, 63 Texas L. Rev. at 14. Here, affirmation of a simple rule—that unilateral price activity does not violate the antitrust laws absent a showing of pricing below average variable cost—will foster competition and give firms the predictability they need to compete.

CONCLUSION

At bottom, this is a simple case. linkLine's "price squeeze" theory rests on the notion that the antitrust laws require the courts to police the margin between the upstream and downstream prices charged by AT&T, its competitor. It is well settled, however, that vertically integrated firms with lawful monopolies in the upstream market may set monopoly prices therein, and that a firm's retail prices will not be found unlawful absent a showing that they are below cost and likely to be recouped at a later date—something respondents failed to allege.

Affirmance of the Ninth Circuit's view of "price squeeze" liability, moreover, would both chill pro-consumer pricing and force the courts into the unfamiliar and uncomfortable role of policing prices. Accordingly, this Court should reverse the judgment of the court of appeals and, in so doing, reaffirm that, regardless of the specific claim involved—be it predatory pricing, price discrimination, bundled discounts, monopoly leveraging, "price squeezes," or other price-based behavior—firms will not be held liable for unilateral pricing decisions absent a showing that they priced their product below average variable cost. Such a decision will ensure that the antitrust laws serve their fundamental purpose, which is "the protection of *competition*, not *competitors*." *Brunswick*

Corp. v. *Pueblo Bowl-O'Mat, Inc.*, 429 U.S. 477, 488 (1977) (quoting *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 320 (1962)) (emphasis added).

For the foregoing reasons, the judgment of the court of appeals should be reversed.

Respectfully submitted,

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SEPTEMBER 2008

AMICUS CURIAE BRIEF

No. 07-512

In The Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
d/b/a AT&T CALIFORNIA, et al.,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., et al.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF OF THE AMERICAN ANTITRUST INSTITUTE AS *AMICUS CURIAE* IN SUPPORT OF DISMISSAL OF THE WRIT OR AFFIRMANCE

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INTEREST OF *AMICUS CURIAE*

The American Antitrust Institute ("AAI") is an independent non-profit education, research, and advocacy organization. Its mission is to advance the role of competition in the economy, protect consumers, and sustain the vitality of the antitrust laws. The Advisory Board of AAI, which serves in a consultative capacity, consists of more than 90 prominent antitrust lawyers, law professors, economists, and business leaders. AAI recently published a major report on the status of U.S. antitrust enforcement, with recommendations for policy on a wide range of topics. *See The Next Antitrust Agenda: The American Antitrust Institute's Transition Report on Competition Policy to the 44th President* (Albert A. Foer ed., 2008), available at http://www.antitrustinstitute.org.[1] AAI submits this brief primarily to urge the Court not to abolish "price squeeze" as an independent basis for antitrust liability, and to demonstrate that this

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[1] The written consent of the petitioners to the filing of this brief is on file with the Clerk. The respondents' consent letter is being filed herewith. No counsel for a party has authored this brief in whole or in part, and no person or entity other than AAI or its counsel has made a monetary contribution to the preparation or submission of this brief. The AAI is managed by its Board of Directors, which alone has approved this filing. The individual views of members of the Advisory Board may differ from the positions taken by AAI. Counsel for respondents, Mr. Blecher, is a member of the Advisory Board but played no role in the Directors' deliberations or the preparation or submission of the brief.

long-established theory remains sound under the Court's modern antitrust jurisprudence.

SUMMARY OF ARGUMENT

1. The writ of certiorari should be dismissed because respondents are no longer asserting a price-squeeze claim, and hence the question presented is merely hypothetical. Further, the absence of real facts makes this case a poor vehicle for making sweeping changes to the existing law on price squeezes.

2. If the Court does not dismiss the writ, the Court should decline the Solicitor General's invitation to decide whether a price squeeze should ever be an independent basis for a violation of Section 2. The question presented does not raise that issue; it is only addressed to the viability of a price-squeeze claim when a determination has been made that a regulated firm has no "antitrust duty to deal." In any event, the well-established rule that a price squeeze may constitute exclusionary conduct under Section 2 is fully consistent with modern antitrust policy and the protection of "competition, not competitors." *Alcoa* and its progeny are best understood as establishing an as-efficient-competitor test that bars a monopolist that operates at two stages of production from foreclosing equally efficient single-stage rivals. The potential anticompetitive effects of a price squeeze by a vertically integrated monopolist, like other forms of vertical foreclosure, are significant and well known.

While a monopolist's extension of its monopoly to adjacent markets could be procompetitive in certain circumstances, there is no reason to think that a rule of reason analysis cannot adequately assess the efficiencies of vertical integration. Moreover, fears of possible overdeterrence do not warrant a rule of per se legality, particularly when the case law generally requires that a plaintiff show not only a price squeeze, but also that the squeeze was deliberate and specifically intended to foreclose competition.

3. Whether the freedom of a monopolist to refuse to deal under the antitrust laws precludes a price-squeeze claim cannot be resolved by pointing out that the latter is no more harmful to competition. The exclusion of a rival by predatory pricing also is no more harmful, yet all parties agree that a *Brooke Group* predatory pricing claim would remain viable. In any event, there are reasons that the "greater" may not include the "lesser" in the unregulated context. Moreover, in a regulated industry where a monopolist is *not* free to refuse to deal, *Trinko*'s rationales for finding no *antitrust* duty to deal do not necessarily apply to a price squeeze of the kind alleged here. The institutional considerations cut differently – the regulatory role of the court is diminished, and the ability and willingness of the FCC to be a good steward of the antitrust function cannot be assumed. Moreover, the inference of predation from the conduct at issue, and the effect on investment in preventing it, are different here than in *Trinko*.

ARGUMENT

I. THE WRIT OF CERTIORARI SHOULD BE DISMISSED

A. The Question Presented Is Moot in Light of Respondents' Abandonment of Their Price-Squeeze Claim

Respondents' brief indicates that they now agree with petitioners and the dissent below that their "pricing squeeze claim survives *Trinko* only if it satisfies the requirements of a predatory retail pricing claim under *Brooke Group*." Resp. Br. 13. Accordingly, they have abandoned their margin-based price-squeeze claim and would have the Court vacate the judgment below. The only claim that they now press is one for conventional predatory pricing under *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). However, given that the issue of whether the complaint states a claim for predatory pricing under *Brooke Group* is not properly before the Court, the writ of certiorari should be dismissed as moot. The question presented at this point is merely hypothetical. *See Deakins v. Monaghan*, 484 U.S. 193, 199 (1988) (where respondents no longer sought certain relief permitted by the court of appeals' decision, question on which certiorari was granted was moot).

B. The Court Should Not Decide a Sweeping Question of Antitrust Policy Without an Adequate Factual Record

The writ should be dismissed for another reason. Petitioners and their *amici* emphasize that the FCC

has completely deregulated DSL broadband transport, having found sufficient "intermodal competition" in broadband Internet access among DSL, cable modem, satellite and wireless broadband. *See* Pet. Br. 4 n.4, 25 n.14. Hence, petitioners suggest that respondents will be unable to prove that petitioners could monopolize high-speed Internet access service. *See id.* at 25 n.14. The dissent made a similar point. *See* Pet. App. 19a-20a. Whether, despite intermodal broadband competition, DSL broadband Internet access is a relevant market in general, as alleged in the complaint, or perhaps in certain geographic markets where cable companies do not operate, is obviously a matter that cannot be determined on the pleadings. However, it would not be prudent for the Court to reach out on an interlocutory appeal to resolve the viability of all or most price-squeeze claims in a case with such a scanty record on this central issue. It is not a good idea to establish antitrust policy (or here, perhaps change decades of accepted antitrust policy) based on abstract theorizing, without being informed by actual facts. *See Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 467 (1992) ("This Court has preferred to resolve antitrust claims on a case-by-case basis,

focusing on the particular facts disclosed by the record.") (internal quotes omitted).[2]

If the writ of certiorari is not dismissed, the judgment of the court of appeals should be affirmed for the reasons set forth below.

II. THE VENERABLE RULE THAT A PRICE SQUEEZE BY A VERTICALLY INTEGRATED MONOPOLIST MAY VIOLATE THE SHERMAN ACT IS CONSISTENT WITH MODERN ANTITRUST POLICY

The Solicitor General argues that a price squeeze by a vertically integrated monopolist should *never* be a basis for liability under Section 2, regardless of whether the industry is fully regulated, partially regulated, or unregulated, and regardless of its effect on competition. *See* U.S. Br. 15, 27. He maintains that victims of a price squeeze may assert a predatory-pricing claim that satisfies the requirement of *Brooke Group*, or a refusal-to-deal claim that satisfies *Trinko*, but a price squeeze should not be an independent basis of liability. *See, e.g.*, U.S. Br. 14 n.8, 25, 29; *see also* Pet. Br. 21 ("Recognition of price squeeze as an independent antitrust tort conflicts with this Court's precedent"). This extreme proposition should be rejected by the Court. While abolishing price-squeeze

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[2] A third reason for dismissing the writ is that the premise of the question presented – that there is no antitrust duty to deal – is hardly free from doubt. *See infra* note 18.

liability is consistent with the Justice Department's "blueprint for radically weakened enforcement of Section 2 of the Sherman Act,"[3] it is beyond the question presented here, as petitioners themselves recognize. *See* Pet. Br. 34. More significantly, it is inconsistent with precedent and sound antitrust policy.

A. *Alcoa* Establishes An Equally-Efficient-Competitor Test

A price squeeze is a form of exclusionary conduct by which a monopolist that operates at two stages of production may foreclose competition from single-stage rivals that purchase an essential input from the monopolist. As the FTC and the appeals court recognized, "Price-squeeze claims have long been part of the Section 2 doctrine . . . ." FTC Statement at 3-4; Pet. App. 14a ("a price squeeze theory formed part of the fabric of traditional antitrust law prior to

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[3] Statement of FTC Commissioners Harbour, Leibowitz and Rosch on the Issuance of the Section 2 Report by the Department of Justice 1 (Sept. 8, 2008), at http://www.ftc.gov/os/2008/09/080908section2stmt.pdf. Notably, the FTC did not join the Solicitor General's briefs in this case, and issued an unusual statement explaining why it disagreed with the Department of Justice's position on the merits and the advisability of certiorari. *See* Statement of the Federal Trade Commission: Petition for a Writ of Certiorari in *Pacific Tel. Co. d/b/a AT&T California v. linkLine Comms., Inc.* (No. 07-512) at 3 (May 23, 2008) (FTC Statement) ("The holding of the Ninth Circuit is unquestionably correct . . . ."); *id.* at 6 ("we do not believe this case is ripe for review").

Trinko"). Judge Hand's landmark *Alcoa* decision,[4] which has been taught to generations of antitrust students, is the leading case on price squeezes, although it was not the first one to conclude that a price squeeze by a vertically integrated monopolist may be unlawful.[5] In the 63 years since *Alcoa,* numerous courts of appeals in addition to the Second Circuit have recognized the viability of price-squeeze claims.[6] The Solicitor General seeks to minimize the force of this well-muscled body of precedent, noting that "the price-squeeze theory of antitrust liability has never been recognized by this Court." U.S. Br. 18. But this Court itself has noted the "add[ed] . . . weight" given to *Alcoa* due to the unique circumstances in which it was decided, *American Tobacco Co. v. United States*, 328 U.S. 781, 811 (1946), and has never questioned the existence of price-squeeze claims. Surely, when Congress enacted the Telecommunications Act of 1996, it would have considered price-squeeze claims to be ones "that satisfy established

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[4] *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945).

[5] *See, e.g., United States v. Corn Products Refining Co.*, 234 F. 964 (S.D.N.Y. 1916).

[6] *See Town of Concord v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990); *Bonjorno v. Kaiser Alum. & Chem. Corp.*, 752 F.2d 802 (3rd Cir. 1984), *cert. denied*, 477 U.S. 908 (1986); *City of Mishawaka v. American Elec. Power Co., Inc.*, 616 F.2d 976 (7th Cir. 1980), *cert. denied*, 449 U.S. 1096 (1981); *City of Kirkwood v. Union Elec. Co.*, 671 F.2d 1173 (8th Cir. 1982), *cert. denied*, 459 U.S. 1170 (1983); *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992).

antitrust standards" that it intended to preserve under the Act's saving clause. *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 406 (2004).[7]

The Solicitor General also denigrates *Alcoa* because Judge Hand spoke of a "fair price" and "living profit," which supposedly indicates a focus on protecting competitors rather than competition. *See* U.S. Br. 24; *id.* at 21 ("*Alcoa* reflects an improper (and, under this Court's decisions, outmoded) focus on the economic well-being of particular competitors"); Pet. Br. 23. But, if the margin available to downstream competitors is insufficient to enable them to compete, then it follows that downstream *competition* will not exist. In any event, as Professor Hovenkamp explains:

> While Judge Hand spoke of the independent fabricator's legal entitlement to a "fair price" from Alcoa, he in fact employed a cost-based test. The test was that the margin between

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[7] The notion that a legal doctrine is not "established law" unless it is endorsed by the Supreme Court is not one that the Court has followed in other areas. *See, e.g., Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 732-33 (1975) (longstanding acceptance by the lower courts of securities law rule established by a decision of Judge Hand, along with Congress' failure to reject the rule, "argues significantly in favor of acceptance of the . . . rule by this Court."); *cf. United States v. Lanier*, 520 U.S. 259, 268-69 (1997) (rejecting position that only a decision of the Supreme Court could satisfy the requirement of fair warning or "clearly established law" for purposes of qualified immunity).

> the price at which Alcoa sold sheet to the independent rollers and its own resale price for rolled aluminum must be at least sufficient to cover the costs that Alcoa itself incurred for the same set of processes. In other words, Judge Hand applied a somewhat primitive version of an "equally efficient rival" test, such as the one that Judge Posner has advocated for unlawful exclusionary conduct assessed under §2 of the Sherman Act.[8]

Other courts have followed this interpretation of *Alcoa* and adopted a "transfer price test" under which a price squeeze is presumed to exist if the monopolist could not have made a profit by selling at its retail rates if it had purchased at its own wholesale rates. *See, e.g., Ray v. Indiana & Michigan Elec. Co.*, 606 F. Supp. 757, 776-77 (D. Ind. 1984); *Illinois Cities of Bethany v. F.E.R.C.*, 670 F.2d 187, 189 (D.C. Cir. 1981); *see also* John Vickers, *Abuse of Market Power*, 115 Econ. J. F244, F251 (2005) (stating that "in principle, if the dominant firm's downstream unit would be loss-making if it paid the wholesale prices charged to rivals, there is a margin squeeze" which prevents "rivals from winning business that they would serve more efficiently than the dominant firm,"

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[8] Herbert J. Hovenkamp & Erik N. Hovenkamp, *The Viability of Antitrust Price Squeeze Claims*, Univ. of Iowa Legal Stud. Res. Paper No. 08-33, at 2-3 (October 2008); *see also* FTC Statement at 4 ("[W]e understand Judge Hand's reference to 'living profit' to be a profit sufficient for participants in the second market to compete.").

and noting that this has been recognized in European case law).

B. The Anticompetitive Effects of a Price Squeeze Are Well Recognized

Petitioners argue that "[t]he fact that 'a one-level monopolist engaged in a prolonged price squeeze may drive independent competitors out of business and thereby extend its monopoly power to a second industry level . . . does not mean that a price squeeze is anticompetitive." Pet. Br 23-24 (quoting *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 23 (1st Cir. 1990)). They refer to the "single monopoly profit" theory popularized by Chicago School scholars, which suggests that "where the wholesale input and the downstream product are in fixed proportion, an upstream monopolist generally cannot earn any greater profits by eliminating an efficient competitor in the downstream market." *Id.* at 24. Petitioners and their *amici* ignore the fact that the assumptions required for the "single monopoly profit" theory are quite restrictive. *See* Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513, 517 (1995). In any event, even when the theory is applicable, "the anticompetitive effects of a price-squeeze scheme can still be significant." FTC Statement at 4.

In *Town of Concord* then-Judge Breyer explained that the principal harms from a monopolist at one level ("upstream") extending its monopoly to a second

industry level ("downstream") are: (1) entry barriers are raised and the upstream monopoly is thereby fortified (leading potentially to higher prices); and (2) non-price competition in the downstream market is eliminated. *See* 915 F.2d at 23-24. The Solicitor General recognizes these harms but seeks to minimize them. *See* U.S. Br. 26-27.

1. Monopoly preservation. As to the entry barriers point, the Solicitor General argues, "Absent formidable preexisting entry barriers upstream, . . . there would be no upstream monopoly." *Id.* at 27. This counterintuitive argument – that additional entry barriers shouldn't matter when the monopoly is entrenched – cannot be taken seriously, for to do so would obliterate the large swath of monopolization law that seeks to prevent monopolists from raising entry barriers. *See Kodak,* 504 U.S. at 485 ("[O]ne of the evils proscribed by the antitrust laws is the creation of entry barriers to potential competitors by requiring them to enter two markets simultaneously.").

Moreover, the entrenchment, or monopoly preservation, concern has been developed beyond the simple "two level entry" problem identified by Areeda & Turner under which a potential entrant in the upstream market would have to enter both the upstream and downstream markets simultaneously because it fears that it otherwise would have no downstream outlets. *See* 3 Phillip Areeda & Donald F. Turner, *Antitrust Law* ¶ 725h, at 204 (1978). More recent authorities emphasize the possibility that

downstream firms themselves may be likely potential entrants in the upstream market[9] or could facilitate entry into the upstream market by increasing the availability of complements to actual or potential competitors.[10]

2. Impairing non-price competition and innovation. The Solicitor General offers that "interfering with the pricing in the marketplace in order to preserve the benefits of non-price competition is not sound antitrust policy, particularly because the second-level firms may not be especially innovative." U.S. Br. 27. He fails to offer any support for this assertion, which seems to reflect no more than the Justice Department's apparent belief in the "Schumpeterian hypothesis" that monopoly is more conducive to innovation than competitive markets. However, the Schumpeterian view is not only contrary to the overwhelming tenor of current economic thinking[11] and is

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[9] *See* Joseph Farrell & Philip J. Weiser, *Modularity, Vertical Integration, and Open Access Policies: Towards a Convergence of Antitrust and Regulation in the Internet Age*, 17 Harv. J. Law & Tech. 85, 111-12 (2003); *see also Town of Concord*, 915 F.2d at 24 ("a 'second-level' independent firm that develops better products or more efficient production methods may thereby obtain the strength needed to challenge the monopolist at the 'primary level.'").

[10] *See* Farrell & Weiser at 109-11.

[11] *See generally* F.M. Scherer & David Ross, *Industrial Market Structure and Economic Performance* 660 (3d ed. 1990) (concluding that "[t]echnological progress thrives best in an environment that nurtures a diversity of sizes and, perhaps, especially, that keeps barriers to entry by technologically

(Continued on following page)

belied by the enormous innovation unleashed by the divestiture of AT&T and its single-stage rivals,[12] it is at odds with the long-held antitrust assumption that "possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone." *Alcoa*, 148 F.2d at 427; *see also American Tobacco*, 328 U.S. at 813 (quoting and endorsing this proposition). Indeed, the problem of innovation in the secondary market is particularly acute in a price-squeeze situation because innovation can be undermined not only by the elimination of rivals but by a squeeze that leaves rivals in business but appropriates their productivity gains. *See* Hovenkamp & Hovenkamp at 17 ("there will be no incentive [by the rival] to reduce costs if the dominant firm can immediately capture the difference by squeezing the smaller firm's margins").

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innovative newcomers low."); William W. Lewis, *The Power of Productivity: Wealth, Poverty, and the Threat to Global Stability* (2004) (survey of studies showing that greater product market competition increases productivity).

[12] *See United States v. W. Elec. Co., Inc.*, 890 F. Supp. 1, 9 (D.D.C. 1995) (decade after breakup "witnessed an unprecedented flowering of innovation"), *vacated as moot*, 84 F.3d 1452 (D.C. Cir. 1996); Farrell & Weiser at 94-95 & n.41 (noting that MCI and Sprint introduced fiber optics, which spurred AT&T to follow).

The elimination of consumer choice in the downstream market is also an antitrust harm. *See, e.g., Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 605-07, 610 (1985) (noting harm from unavailability of all-Aspen ticket, which deprived consumers of ability to "make their own choice on these matters of quality"); *see generally* Neil W. Averitt & Robert H. Lande, *Using the "Consumer Choice" Approach to Antitrust Law*, 74 Antitrust L.J. 175 (2007). This loss of choice may be particularly harmful in the broadband Internet context, where ISPs have the ability to discriminate against certain types of content otherwise available on the Internet. *See Network Access, Regulation and Antitrust* 151, 159-60 (Diana L. Moss ed., 2005).

3. Facilitation of price discrimination. The monopolist's extension of its monopoly to the secondary market may also be harmful insofar as it facilitates price discrimination, which is itself an exception to the single monopoly profit theory. While some scholars maintain that price discrimination can be procompetitive or at least has indeterminate welfare effects, the Court has treated it as an anticompetitive consequence of exclusionary conduct by a monopolist. *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 14-15 & n.23 (1984) ("impairment of competition" from tying includes "increas[ing] the social costs of market power by facilitating price discrimination, thereby increasing monopoly profits over what they would be absent the tie"); *see also* Barry Nalebuff, *Unfit to be Tied. An Analysis of* Trident v.

Independent Ink, *in The Antitrust Revolution* (John E. Kwoka, Jr. & Lawrence J. White eds., 5th ed. 2008) (price discrimination typically will lead to reductions in consumer welfare). At the least, there is no reason to assume that a price squeeze designed to facilitate price discrimination is procompetitive.

4. Fixed-proportions assumption is generally not realistic. A fundamental assumption of the single monopoly profit theory is that the monopoly product and the secondary product are used in fixed proportions. However, "[v]ariable proportions cases are quite common . . . ." Robert H. Bork, *The Antitrust Paradox* 229 (1978). And in variable proportions cases, "under plausible circumstances, vertical integration downstream by an input monopolist *can* lead to enhanced monopoly power and price increases." Scherer & Ross at 525. Relatedly, the single monopoly profit theory does not apply when the complementary product in the secondary market is not a complete complement; that is, some consumers may consume the rival's product without the primary product (or, at least, the primary product sold by the monopolist). If that is the case, and there are economies of scale in the production or consumption of the secondary product, then vertical foreclosure may prevent the rival from reaching efficient scale, and consumers of the "standalone" secondary product may be harmed.

See Michael D. Whinston, *Tying, Foreclosure, and Exclusion*, 80 Am. Econ. Rev. 837 (1990).[13]

5. Regulation "exception" to single monopoly profit theory. Another well-recognized "exception" to the single monopoly profit theory is when there is price regulation at the primary level. *See Town of Concord*, 915 F.2d at 29 ("We recognize that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first."); 3A Phillip E. Areeda & Herbert Hovenkamp, *Antirust Law* ¶ 787b, at 298 (2d ed. 2002) ("[F]ull monopoly profit can usually be obtained by monopoly at one stage, and the monopolist would have no reason further to restrict output by raising

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[13] Petitioners baldly assert that this case involves fixed proportions, *see* Pet. Br. 24, but this assertion seems belied by the suggestion that ISPs can reach customers over other platforms, such as cable and satellite. *See* Pet. Br. 4 n.4. *Cf. Kodak*, 504 U.S. at 463 (explaining that functionally linked products that may not be used without one another may constitute separate product markets). In any event, while an ISP may depend on a particular DSL broadband transport provider to reach customers in one local market, it does not necessarily depend on the same provider in each local market. Moreover, ISPs offer ancillary services (*e.g.*, e-mail, content, portals, and applications) that are not used in fixed proportions with DSL transport service. *See* Barbara van Schewick, *Towards an Economic Framework for Network Neutrality Regulation*, 5 J. on Telecomm. & High Tech. L. 329, 350-52, 356 (2007) (suggesting that ancillary services may be available on a standalone basis and subject to economies scale).

the price at the stage into which it integrated. Regulation changes the picture in that significant respect.").

The Solicitor General acknowledges that petitioners' wholesale rates for DSL transport were subject to regulation by the FCC, but misses the potential import of this regulation when he contends that "if . . . there is no sound basis to treat margin-based price squeezes as antitrust violations even in unregulated markets, there is surely no reason to do so in wholly or partly regulated markets." U.S. Br. 28. Such a proposition would surely have startled Professor Baxter and other classical Chicago School adherents. *See* Farrell & Weiser at 105-07 (describing regulated monopoly exception to single monopoly profit theory as "Baxter's Law" because it was at the heart of the government's antitrust case against AT&T). Similarly, the Solicitor General errs in asserting that the prospect of earning monopoly profits at the second level "is essentially a problem of regulatory evasion, not of antitrust law" and that the FCC can police a price squeeze even though it does not regulate retail rates. *Id.; see also* Pet. Br. 37. "[T]he relevance of rate regulation avoidance is not that antitrust appropriately supervises rates, but that avoiding rate regulation is the profit motive that might induce the price-regulated firm to engage in conduct that excludes others from an adjacent market otherwise open to competition." 3A Areeda & Hovenkamp ¶ 787b, at 301. Whether antitrust should stay its hand because regulators can appropriately

police a price squeeze in a partially regulated industry is a separate question.

6. Complete exclusion unnecessary. It is worth emphasizing that the harms from vertical foreclosure strategies such as a price squeeze do not necessarily require that the monopolist completely exclude the rival from the downstream market. Rather, simply raising the rival's costs and thereby marginalizing it may have effects similar to complete exclusion. *See generally* Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs To Achieve Power over Price*, 96 Yale L.J. 209 (1986). Furthermore, at least one important anticompetitive situation depends on the rival firm's *not* exiting the market, namely when the monopolist misappropriates the rival's fixed-cost investments by squeezing it just enough to keep it in business.[14]

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[14] Professor Hovenkamp, while noting the effect of such a squeeze in reducing the incentives of rivals to innovate and reduce costs, has questioned whether this should constitute anticompetitive behavior "despite the somewhat malicious nature of this sort of price squeeze." Hovenkamp & Hovenkamp at 17. *But see* Herbert Hovenkamp, *Antitrust Policy After Chicago*, 84 Mich. L. Rev. 213, 267-68 (1985) ("[T]he antitrust laws can encourage efficient investment by protecting firms from strategic, inefficient advantage-taking by others."); *id.* at 269 ("price squeeze may often be a mechanism by which a monopolist takes advantage of a vertically related firm's sunk investment in order to force an infracompetitive rate of return on the firm").

7. Procompetitive justifications. The monopolist's extension of its monopoly could be procompetitive in certain circumstances. *See Town of Concord*, 915 F.2d at 24-25 (citing avoidance of double marginalization in particular). Moreover, a price squeeze that excludes an as-efficient downstream competitor could be the result of efficiencies of vertical integration (*e.g.*, if it is more costly for the monopolist to serve its rivals than itself). But any rule of reason analysis would take procompetitive justifications into account. *See, e.g., United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (D.C. Cir. 2001) (articulating a structured rule of reason for Section 2). Petitioners assert that it "would always be difficult for an adjudicator to distinguish a price squeeze resulting from [superior] efficiency from a price squeeze resulting from supposedly excessive wholesale prices," Pet. Br. 27, but the *Alcoa* test screens out efficiencies at the secondary level, and petitioners offer no evidence to believe that the assessment of other efficiencies is more difficult for price squeezes than other types of exclusionary conduct. *See, e.g., Energex Lighting Industries, Inc. v. N. American Philips Lighting Corp.*, 765 F. Supp. 93, 105 (S.D.N.Y. 1991) (dismissing price-squeeze claim where the squeeze "resulted from Philips being a more efficient company").

B. Fear of Possible "Overdeterrence" Should Not Bar Price-Squeeze Claims

1. Innocent price squeezes are not illegal. Petitioners and their *amici* maintain that recognition

of price-squeeze claims would deter procompetitive conduct by discouraging aggressive retail pricing or efficient vertical integration by the monopolist. *See* Pet. Br. 27-28; *see also* U.S. Br. 24. For example, the argument goes, a monopolist may wish to reduce retail prices because of changing demand conditions in the retail market, yet may refrain from doing so because it would feel compelled to lower wholesale prices as well, lest it be sued for having engaged in an unlawful price squeeze. Neither the petitioners nor any of the *amici* have cited any empirical or even anecdotal evidence that vertically integrated monopolists have been deterred from legitimate price cutting because of a fear of price-squeeze liability. And for good reason. Courts have held that a mere price squeeze by a monopolist does not violate Section 2. *See Antitrust Law Developments* 287 (6th ed. 2007). For example, the Third Circuit has required proof that the squeeze was deliberate and "not the result of natural market forces such as supply and demand or legitimate competition." *Bonjorno*, 752 F.2d at 809. Other courts have required a showing that the monopolist had a specific anticompetitive intent or lacked a legitimate business justification. *See City of Anaheim*, 955 F.2d at 1378-79; *City of Mishawaka*, 616 F.2d at 985.[15] To be sure, any rule other than per

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[15] Petitioners themselves suggest another reason that low retail pricing is unlikely to be deterred by potential price-squeeze liability: the risk that raising retail prices will be construed as collusion with the downstream rival. *See* Pet. Br. 27 n.16.

se legality runs the risk of some "false positives." However, concerns about overdeterrence will be minimized by placing the burden on plaintiffs to allege and prove not only that the integrated monopolist's price squeeze does not permit an equally efficient rival to survive but also that the price squeeze was specifically intended to foreclose competition from unintegrated rivals.

2. *Alcoa* test is consistent with *Brooke Group*. *Brooke Group* does not require a different result. The Solicitor General correctly points out that *Brooke Group* rejected above-cost predatory pricing claims, even though the Court acknowledged that such conduct could be anticompetitive, because "the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator . . . or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting." *Brooke Group,* 509 U.S. at 223. Neither rationale supports eliminating price squeeze liability. The first rationale is wholly inapplicable because the *Alcoa* test for liability focuses precisely on whether an equally efficient competitor would be excluded (notwithstanding that the elimination of a less efficient competitor could also be anticompetitive). The second rationale is also inapt because *Alcoa*'s cost-based safe harbor, along with the specific intent requirement, provides sufficiently clear guidance to monopolists and courts so as not to unduly chill legitimate price

cutting. *See* FTC Statement at 4 (*Alcoa* test "is at least as clear as the undefined 'below-cost' standard in *Brooke Group*").

The mere fact that the exclusionary conduct in a price squeeze involves prices does not mean that an orthodox *Brooke Group* standard should apply. The treatment of bundled discounts provides a good analogy. A bundled discount involves situations in which a monopolist sells a monopolized product and a competitive product, and offers a discount to customers that buy both products instead of the monopolized product separately, which single-product rivals may not be able to match. Some commentators have argued that such discounts should only be actionable when the price of the product bundle is less than the incremental cost of producing the two products under *Brooke Group*, because otherwise discounting will be chilled. Yet a number of courts (including the Ninth Circuit in a decision written by Judge Gould),[16] the Antitrust Modernization Commission, and even the Justice Department have rejected the *Brooke Group* test for bundled discounts in favor of a "discount attribution rule," which would potentially allow for liability when the "imputed" price of the competitive product (after allocating all discounts to the competitive product) is below the monopolist's incremental costs of producing that product, even if the price of

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[16] *See Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2008).

the bundle exceeds the incremental costs of the two products.[17]

The rationale for the discount-attribution rule for bundled discounts is that pricing that does not satisfy this test would exclude an equally efficient single-product competitor, and the rule provides sufficient clarity to businesses and courts so as not to unduly chill procompetitive discounting. Likewise, the *Alcoa* rule, which potentially allows for liability when the price of the competitive product minus its "imputed" wholesale cost is below the monopolist's incremental retail (or downstream) costs, would permit as-efficient retail competitors to compete, and provide sufficient clarity.

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Ultimately, the Solicitor General's arguments for abolishing price-squeeze liability reflect a deep skepticism about the harmfulness of vertical foreclosure strategies by monopolists, and an unwarranted fear of "false positives." And while this policy predilection has been a part of the antitrust debate for decades, the Court has quite properly never accepted it as a basis for immunizing vertical foreclosure from antitrust scrutiny, and should not do so here.

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[17] *See* U.S. Dept. of Justice, *Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act* 91-102 (2008) (describing alternative rules).

III. THE DISTRICT COURT'S DETERMINATION THAT PETITIONERS HAD NO "ANTITRUST DUTY TO DEAL" DOES NOT BAR RESPONDENTS' PRICE-SQUEEZE CLAIM

Petitioners maintain that where, as here, the district court determined that there was no "antitrust duty to deal" under *Trinko*,[18] it follows that a price-squeeze claim cannot be maintained because a price squeeze cannot be any more anticompetitive than an

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[18] Whether petitioners had a duty to deal under *Aspen* and *Trinko was* disputed on appeal, *see* Brief of Appellees 21-23, contrary to petitioners' assertion. *See* Pet. Br. 19. What was not disputed was that petitioners were required by law to offer DSL transport facilities as long as they provided DSL Internet service at retail. *See* Pet. App. 5a n.6, 85a. Petitioners assert that there was no basis for any argument that they "'would ever have [provided DSL transport facilities to respondents] absent statutory compulsion,'" Pet. Br. 19 (quoting *Trinko*), but they (and other incumbent local exchange carriers) made precisely the opposite contention to the FCC in seeking to have the regulatory requirements lifted. *See Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853, 14893, ¶ 74 n.223 (2005) (*Wireline Broadband Framework Order*) ("SBC will continue to enter into ISP broadband access arrangements as a way of increasing subscriber growth and utilization of its broadband network *regardless of any regulatory compulsion to do so*.") (quoting SBC July 31, 2003 *Ex Parte* Letter at 8) (emphasis added). Indeed, the FCC found these arguments to be a persuasive reason to lift regulation. *See id.* at 14892-94, ¶¶ 74-75. Neither the district court nor the appeals court considered respondents arguments that "charging rivals higher prices than otherwise available to consumers, falls within the exception to the general 'no duty to deal' rule carved out by *Aspen Skiing* and *Otter Tail*." Brief of Appellees 22.

outright refusal to deal. *See* Pet. Br. 34; *see also* U.S. Br. 14 ("A defendant that has no duty to deal with rivals by definition has no duty to deal with them on particular terms that would permit them to compete."); *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673 (D.C. Cir. 2005) ("it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal") (quoting 3A Areeda & Hovenkamp ¶ 767c5, at 129-30). This argument fails for a number of reasons.

A. The Fact That a Price Squeeze May Be No More Harmful to Competition Than a Refusal to Deal is Not Dispositive

As an initial matter, the equal-harm-to-competition argument proves too much because it would bar a *Brooke Group* predatory pricing claim as well – exclusion of a downstream rival from the market using predatory pricing or a refusal to deal (or any other foreclosure technique for that matter) has the same effect on competition.[19] And under the "single monopoly profit" theory relied upon by petitioners, recoupment would be impossible because the monopolist can earn no greater profits by integrating downstream. Moreover, as Professor Hovenkamp

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[19] Indeed, consumer harm from vertical foreclosure due to predatory pricing should be less than from a refusal to deal because at least with predatory pricing consumers get to enjoy a period of below-cost pricing before the rival is eliminated.

asks, "Why would the dominant firm undergo a costly period of predatory pricing when it could destroy the rival simply by refusing to deal?" Hovenkamp & Hovenkamp at 13. Yet, petitioners and the Solicitor General maintain that a *Brooke Group* predatory pricing claim would be viable, if properly alleged. *See* Pet. Br. 8; U.S. Br. 15-17.

Second, it is important to distinguish between antitrust duties to deal in the regulated and unregulated contexts. The district court's determination of "no antitrust duty to deal" was premised on the existence of regulation. The Court need not and should not decide the extent to which the hypothetical absence of an antitrust duty to deal would preclude a price-squeeze claim in the unregulated context. Indeed, even in the refusal to deal context, as in *Aspen Skiing*, the Court does not ask whether there is some abstract "antitrust duty to deal," but rather asks whether a refusal to deal by a monopolist in given circumstances gives rise to antitrust liability. In any event, as a matter of logic and policy it does not follow that if a monopolist may lawfully refuse to deal with a downstream rival, it should be free to harm the rival in other, perhaps less drastic ways, such as a price squeeze. The lesser-within-the-greater argument is unsound in many areas of the law,[20] including antitrust. For example, the *Colgate* doctrine

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[20] *See, e.g., 44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 510-11 (1996) (Stevens, J.) (commercial speech).

permits a manufacturer to refuse to deal with a retailer that fails to adhere to the manufacturer's suggested retail prices, but does not necessarily permit less drastic measures such as suspending the retailer for a short period. *See* Brian R. Henry & Eugene F. Zelek, Jr., *Establishing and Maintaining an Effective Minimum Resale Price Policy: A* Colgate *How-To*, Antitrust, Summer 2003, at 8, 10; *United States v. Parke, Davis & Co.*, 362 U.S. 29, 44 (1960). The *Colgate* doctrine and *Trinko* are founded upon "'the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.'" *Trinko*, 540 U.S. at 408 (quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)). But the same solicitude does not necessarily apply to a monopolist's determination to eliminate or neuter an existing customer/rival through a price squeeze. And, a rational antitrust policy might consider that a monopolist bluntly cutting off a rival would be problematic but relatively unlikely to occur because it requires the monopolist to forego wholesale revenues, or because it is too drastic an option, or because it would raise contractual, regulatory, or reputational risks, whereas a price squeeze might be more likely to be used (perhaps because it is less obvious) and therefore warrant greater antitrust scrutiny. *See, e.g.*, Riordan & Salop at 535 n.55 (noting that refusing to deal may be less effective than raising rivals' costs).

B. *Trinko*'s Rationale Does Not Apply to the Price Squeeze Alleged Here

Petitioners, of course, were not "free to refuse to deal" with respondents. As in *Trinko*, such a refusal to deal would have violated telecommunications law. However, the factors in *Trinko* that led the Court to conclude that defendant's refusal to deal did not also violate Section 2 do not apply to a price squeeze of the type alleged here. The Court was reluctant to impose an antitrust duty to deal not because a refusal to deal by a monopolist in one market controlling an essential input for rivals to compete in an adjacent market is competitively harmless. (Indeed, *Trinko* was not a classic vertical-foreclosure or monopoly-leveraging case at all.) Rather, institutional concerns were paramount. The Court was concerned that "[a]n antitrust court is unlikely to be an effective day-to-day enforcer of . . . detailed sharing obligations." *Trinko*, 540 U.S. at 415; *see id.* at 408 ("Enforced sharing . . . requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill suited."). At the same time, the regulatory "regime was an effective steward of the antitrust function." *Id.* at 413; *see id* at 412 ("One factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm."). Indeed, the "enforcement scheme set up by the 1996 Act [was] a good candidate for implication of antitrust immunity. . . ." *Id.* at 406. These institutional factors cut differently in the case of a price squeeze.

1. The role of the court. The "regulatory" role of the court in a price squeeze is significantly lessened because the retail price offered by the monopolist provides a benchmark for determining the wholesale price. Indeed, in the case of a discriminatory price squeeze like the one alleged here, where the wholesale price allegedly exceeded the retail price, *see* J.A. 35, the court does not have to determine the price of access at all; it can provide an adequate remedy merely by ordering the monopolist not to discriminate in its treatment of rivals and other customers, *e.g.*, charge no more for wholesale DSL transport than for retail DSL Internet service.[21] *See Town of Concord,* 915 F.2d at 28 (noting that in cases where price squeeze allegations involve wholesale prices that exceed retail prices "some of the 'administrative' problems we have found surrounding a jury's efforts to determine the reasonableness of the price 'gap'" are eliminated); *Trinko*, 540 U.S. at 410 n.3 (distinguishing concerted refusals to deal in part because they are "amenable to a remedy that does not require judicial estimation of free market forces: simply requiring that the outsider be granted nondiscriminatory access to the club"). As counsel for Verizon has elsewhere suggested, the "institutional task for courts is much more manageable" in a discrimination situation because "[t]he voluntary sales to others furnish a standard of conduct – equality – that the

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[21] Other remedies, such as damages or divestiture, do not require any supervision of rates at all.

courts do not have to define on their own." John Thorne, *A Categorical Rule Limiting Section 2 of the Sherman Act:* Verizon v. Trinko, 72 U. Chi. L. Rev. 289, 299 (2005).[22]

2. The effectiveness of regulatory remedies. It is not clear, at least on this record, that the FCC is an adequate steward of the antitrust function. Broadband Internet service has long been considered an "information service" not subject to common carrier regulation by the FCC; hence the FCC did not regulate retail DSL rates.[23] To be sure, the FCC presumably had the authority to address a price-squeeze complaint pursuant to its jurisdiction to determine whether a carrier's wholesale rates are "just and reasonable."[24] However, *Trinko* did not hold

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[22] Petitioners and their amici suggest that the wholesale-greater-than retail situation is not as straightforward as it appears because the retail service may involve ancillary revenues from advertising or from increased sales of bundled offerings. *See* Pet. Br. 32-33 n.21. However, the same complications arise in the predatory pricing context when "below cost" sales of the predatory product may be offset by increased revenues from advertising or sales of complementary products.

[23] *See Wireline Broadband Framework Order*, 20 FCC Rcd at 14927, ¶ 136.

[24] *See Application by SBC Communications Inc., Pacific Bell Telephone Company, and Southwestern Bell Communications Services Inc., for Authorization To Provide In-Region, InterLATA Services in California*, 17 FCC Rcd 25650, 25736-37, ¶ 156 & n.562 (2002) (rejecting price-squeeze complaint regarding DSL transport service as inappropriate in § 271 proceeding, and noting that the appropriate venue for such allegations is a complaint under § 208 of the Act). Notably, in *Town of Concord*,

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that the mere possibility of regulatory action was sufficient to deter and remedy anticompetitive harm. On the contrary, in *Trinko* the FCC (and state regulators) had *in fact* remedied Verizon's breach of its network-sharing duties with a consent decree, fines, and other penalties. *See* 540 U.S. at 412-13; *see also Credit Suisse Sec. (USA) LLC v. Billing*, 127 S. Ct. 2383, 2396 (2007) (finding implied immunity where "the SEC actively enforces the rules and regulations that forbid the conduct in question" and private litigants had obtained damages under securities laws for the type of conduct at issue); *cf. Town of Norwood v. New England Power Co.*, 202 F.3d 408, 419 (1st Cir. 2000) (holding price-squeeze claim barred by filed rate doctrine where FERC had addressed plaintiff's competitive concerns). And in *Otter Tail*, the Court concluded that antitrust remedies were appropriate even where the regulatory agency had provided at least partial relief. *See Otter Tail Power Co. v. United*

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then-Judge Breyer recognized the authority of the FERC to remedy a price squeeze under *FPC v. Conway*, but nonetheless would not foreclose the possibility of price-squeeze liability when the second level is unregulated. *See Town of Concord*, 915 F.2d at 28, 29. The reason that "full" regulation barred price-squeeze claims in *Town of Concord* was not merely the existence of an administrative remedy, but the pervasive regulation of rates, entry, and change of control that "significantly diminish[ed] the likelihood of major antitrust harm," and the potential conflict between antitrust liability and the regulatory scheme. *See id.* at 25-28; *see also id.* at 22 ("in light of regulatory rules, constraints, and practices, the price squeeze at issue here is not ordinarily exclusionary").

States, 410 U.S. 366, 372 (1973) (Federal Power Commission had ordered utility to interconnect and sell power at wholesale to rival, but lacked the authority to order wheeling; noting that "[a]ctivities which come under the jurisdiction of a regulatory agency nevertheless may be subject to scrutiny under the antitrust laws."); *see also United States v. AT&T*, 552 F. Supp. 131, 168 (D.D.C. 1982) (ordering breakup of Bell System where FCC regulation had been ineffective). Indeed, the Solicitor General asserts, "Regulatory enforcement should not displace antitrust enforcement unless the criteria for implied immunity are satisfied." U.S. Br. 15.

Here, the Commission's practical ability and willingness to remedy a price squeeze are open to question. The Commission itself has noted that its ability to police a price squeeze involving wholesale tariffed rates is limited when, as here, rates are not reviewed in advance. *See Unbundled Access to Network Elements*, 20 FCC Rcd 2533, 2569-70, ¶ 62 (2005) (expressing concern that possible post hoc relief "would not be sufficient to prevent harm in the first instance to competitors relying on a wholesale input priced to effect a price squeeze").[25] Moreover,

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[25] In theory, DSL transport rates were required to be offered pursuant to tariff until rates were completely deregulated in 2005. However, even before 2005 the regulation of rates was limited. From 2000 to 2001, SBC offered DSL transport as a non-dominant carrier "under contract," and not under tariff. *See Regulatory Review of Requirements for Incumbent LEC Broadband Telecommunications Services*, 17 FCC Rcd 27000,

(Continued on following page)

the Commission's zest to deregulate broadband markets suggests that a price squeeze claim may have little traction. *See, e.g.*, Harvey Reiter, *The Contrasting Policies of the FCC and FERC Regarding the Importance of Open Transmission Networks in Downstream Competitive Markets*, 57 Fed. Comm. L.J. 243, 318-19 & n.389, 321 (2005) (maintaining that FCC has been indifferent to ISP complaints about exclusionary practices and that its "obliviousness to downstream competition issues has led it to ignore alternatives to the deregulatory course it has chosen"). In all events, the adequacy of the regulatory stewardship of the antitrust function should not be presumed. *See* Philip J. Weiser, *The Relationship of Antitrust and Regulation in a Deregulatory Era*, 50 Antitrust Bull. 549, 558 (2005).

3. Incentives for investment, and inferences of predatory intent. The Court in *Trinko* was also concerned about the disincentives for investment that it believed may result from "enforced sharing." *Trinko*, 540 U.S. at 407-08 ("Compelling [monopolists] to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentives for the monopolist, the rival, or both to invest in these economically

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27002-03, ¶¶ 3-5 (2002). Beginning in September 2001, it filed tariffs, but cost support and notice requirements were waived. *See id.* at 27003 n.18. Subsequently, the FCC granted SBC's petition for forbearance from tariffing requirements. *See id.* at 27008, ¶ 13.

beneficial facilities.").[26] Petitioners reprise that argument here. *See* Pet. Br. 29-30. But prohibiting a monopolist from squeezing a rival is unlikely to undermine incentives as long as the retail price chosen by the monopolist is otherwise profitable. *See* Thorne at 298-99 (noting that "there is much less reason to worry about deterring long-run and short-run investments by requiring the results to be shared" on terms the monopolist voluntarily offers to others); Einer Elhauge, *Defining Better Monopolization Standards*, 56 Stan. L. Rev. 253, 310 (2003) (arguing that barring monopolist from discriminating on the basis of rivalry does not undermine *ex ante* incentives).

Relatedly, the Court in *Trinko* found it significant that "the services allegedly withheld are not otherwise marketed or otherwise available to the public" and "exist only deep within the bowels of Verizon," in contrast to *Aspen* "where the defendant refused to provide to its competitor . . . a product that it already sold at retail" and to *Otter Tail* where Otter Tail

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[26] This concern has been questioned by commentators who note among other things that: (1) the monopolist's incentives depend upon the provenance of the monopoly facility and the price of access; (2) providing access to the rival may make it more likely that it will invest in beneficial facilities in the monopoly market in the future; and (3) access may increase the incentives of the rival (and the monopolist) to invest in the adjacent or complementary market. *See, e.g.*, Brett Frischmann & Spencer Weber Waller, *Revitalizing Essential Facilities*, 75 Antitrust L.J. 1, 32-36 (2008).

refused to provide the same service to its rival that it provided to "certain other customers." *Trinko*, 540 U.S. at 410. The Court said that "Verizon's reluctance to interconnect at the cost-based rate of compensation available under § 251(c)(3) tells us nothing about dreams of monopoly," while Aspen Skiing's discriminatory treatment of its rival "revealed a distinctly anticompetitive bent." *Id.* at 409. *See* Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Petitioner 23 n.8, *Trinko*, 540 U.S. 398 (2004) (No. 02-682) ("The monopolist's willingness to offer non-competitors particular terms is evidence that those terms are profitable to it, and that the refusal to offer the same terms to competitors represents a sacrifice of immediate profits that would not make sense but for the tendency to impair competition."); Thorne at 298 ("[I]f you are selling this to others at a price that is profitable and lets you recoup your investment, what reason is there for not selling the same thing at the same price to a rival?").

Unlike the defendant in *Trinko*, but like *Aspen* and *Otter Tail*, petitioners offered DSL transport service not merely to rivals (and certainly not at any mandated low-cost rates), but to the public as well and refused to provide it to its competitors on the same terms. Petitioners argue that what they supplied to the public was not DSL transport, but "something different – DSL-based Internet-access service . . . ." Pet. Br. 20 n.11; *see also* U.S. Br. 14 n.7 ("the complaint contains no suggestion that respondents ever sought, or desired, to purchase from

petitioners the bundled Internet access service (incorporating DSL transport) that petitioners sold at retail"). However, the fact that petitioners offered consumers *more* than just DSL transport, while charging less for the bundle than they charged rivals for just DSL transport, only makes the discrimination more apparent and thus the inference of predatory intent only stronger.

In sum, the institutional considerations and inferences of predatory intent that arise in connection with refusals to deal do not apply in the same fashion to price squeezes of the kind alleged here. Hence the district court's finding of "no antitrust duty to deal" should not preclude respondents' price-squeeze claim.

CONCLUSION

For the foregoing reasons, the writ of certiorari should be dismissed or the judgment of the court of appeals should be affirmed.

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AMICUS CURIAE BRIEF

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In The
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
d/b/a AT&T CALIFORNIA, ET AL.,

Petitioners,

v.

INKLINE COMMUNICATIONS, INC., ET AL.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF OF THE COMMONWEALTH OF VIRGINIA AND EIGHT OTHER STATES AS AMICI CURIAE IN SUPPORT OF THE PETITIONERS

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INTEREST OF AMICI

The interests of the States are twofold. First, because the States are among the leading enforcers of antitrust law, they have a compelling interest in ensuring the soundness and uniformity of antitrust jurisprudence. The lower court created a conflict among the Circuits and announced an exception to *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004). The States need resolution of this conflict and also want an interpretation that is rational and predictable—a price-squeeze claim may not be brought against a firm that has no antitrust duty to deal. Such a bright-line rule will encourage and support competition, innovation, and growth in the marketplace, for the ultimate benefit of consumers.

Second, the States have a critical interest in preserving the efficiency and the integrity of their marketplace by reducing costs associated with unfounded lawsuits. Businesses in the United States face the highest legal costs in the industrialized world.[1] Antitrust litigation imposes significant

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[1] According to the Office of Management and Budget, "[t]he costs of litigation per person in the United States are far higher than in any other major industrialized nation in the world. Lawsuit costs have risen substantially over the past several decades, and a significant part of the costs go to paying lawyers' fees and transaction costs—not to compensating the injured parties." *Promoting Economic Opportunity and Ownership*, OFF. OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2006 (2005),

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burdens on businesses, the courts, and our economy. *Trinko*, 540 U.S. at 414-15. If, as the Ninth Circuit held, an antitrust plaintiff can state a price-squeeze claim even though the defendant has no duty to deal, then businesses will face more litigation. Businesses will be prompted to settle these cases, even at a high cost, to avoid extraordinarily high discovery costs and the uncertainties of litigation. These expenses will ultimately be passed on to consumers.

SUMMARY OF ARGUMENT

The decision below should be reversed for three reasons. First, the Ninth Circuit's decision is contrary to the interest of consumers. The decision below, by protecting competitors rather than competition, would have undesirable effects for consumers. To avoid costly antitrust litigation, companies may avoid price-cutting or refuse to enter a downstream market. This would deprive consumers of choice and competition. Second, determining a wholesale price that is fair relative to retail pricing is an exercise for which courts are ill-suited. Setting a wholesale price depends on the characteristics of a specific market and therefore, defining a rule would be arbitrary and

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available at http://www.whitehouse.gov/omb/budget/fy2006/promoting.html.

difficult to administer. Finally, the reasoning in *Trinko* is incompatible with the ruling below.

I. THE NINTH CIRCUIT'S DECISION UNDERMINES THE INTERESTS OF CONSUMERS.

Regarded as "the Magna Carta of free enterprise," *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 610 (1972), the Sherman Act[2] seeks to prohibit the acquisition or maintenance of monopoly power—the power to control prices or exclude competition—by means other than growth or development as a consequence of a superior product, business acumen, or historic accident. *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966). Because a monopolist may have less incentive to reduce prices, improve quality, or offer greater selection, this rule reflects the general principle that the antitrust laws "were enacted for the protection of *competition* not *competitors*." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (emphasis original, internal quotations omitted). Competition ultimately benefits consumers in the form of lower prices, higher quality, and larger selection.

The Ninth Circuit's decision undermines these principles in two ways. First, it protects competitors

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[2] 15 U.S.C § 2.

rather than competition. Second, it penalizes companies for cutting prices.

A. The Decision Below Protects Competitors Rather Than Competition.

The decision below protects competitors—the downstream rivals who are upset by the firm's pricing policies—rather than the competition of the marketplace. If a business faces potential liability for a "price squeeze," even though it has no antitrust obligation to deal with its downstream competitors, then it will be reluctant to engage in pro-competitive behavior that might prompt a lawsuit by its downstream competitors. *See* William J. Baumol & Janusz A. Ordover, *Use of Antitrust To Subvert Competition,* 28 J.L. & ECON. 247, 254 (1985). Most obviously, it may shy away from vertical integration by refusing to enter the downstream market. For businesses that are vertically integrated, one way to avoid a price-squeeze lawsuit would be to charge higher downstream prices.[3] Alternatively, it might refuse to sell at the wholesale level or at the retail level to avoid an easily alleged complaint of a price

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[3] A lower downstream price most often reflects competition rather than a sinister attempt at a price squeeze. In this particular market, consumers can gain access to the internet via DSL, cable, satellite and a wireless connection. Thus, maintaining low downstream prices simply reflects price pressure from these DSL alternatives.

squeeze. All of these actions would reduce competition and, in the long run, harm consumers.

Similarly, because there is a "long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal," *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919), a vertically integrated firm simply may refuse to sell its upstream products to its downstream competitors. Such a development would remove any economic efficiency that might result from such sales. *See* 3A Phillip Areeda & Harold Hovenkamp, ANTITRUST LAW § 767 c.3 (2nd ed. 2002). Production costs for downstream firms then would be higher. Those higher production costs inevitably would be passed on to consumers in the form of higher prices.

Vigorous competition is good for consumers, but bad for those companies that are the weakest in the marketplace. William J. Baumol & Alan S. Blinder, ECONOMICS: PRINCIPLES & POLICY 275 (10th ed. 2006). Indeed, "it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal." *Covad Commc'ns Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673 (D.C. Cir. 2005) (quoting 3A Phillip Areeda & Harold Hovenkamp, ANTITRUST LAW § 767 c.5).

The Ninth Circuit's decision allows the weak companies to chill the behavior of stronger ones to the detriment of consumers. *See Trinko*, 540 U.S. at 414.

The Magna Carta of free enterprise does not mandate such a result.

B. The Lower Court Decision Penalizes Businesses For Above-Cost Price Cutting.

The lower court decision penalizes companies for above-cost price cutting. This Court has been "particularly wary of allowing recovery for above-cost price cutting because allowing such claims could, perversely, 'chill legitimate price cutting, which directly benefits consumers.'" *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1074 (2007) (citation omitted). Consumers benefit from lower prices "regardless of how these prices are set, and so long as they are above predatory levels, they do not threaten competition." *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990). Condemning practices resulting in lower prices to consumers is thus "especially costly" because "cutting prices in order to increase business often is the very essence of competition." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986). As this Court observed:

> the purpose of the [Sherman Act] is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself.

> It does so not out of solicitude for private concerns but out of concern for the public interest.

Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993).

II. THE COURT OF APPEALS' DECISION WILL PROVE DIFFICULT TO ADMINISTER.

Even if the court of appeals' price-squeeze theory were sound, it still should be rejected in light of the difficulty courts would have administering the test the theory requires. As then Judge, now Justice Breyer, explains:

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will?

Town of Concord v. Boston Edison Co., 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, J.). These difficulties explain "why antitrust courts normally avoid direct price administration." *Id.*[4] The assumption of "day-to-day controls characteristic of a regulatory agency"[5] that the court of appeals' rationale requires, would promote needless litigation and uncertainty.

III. THE NINTH CIRCUIT'S DECISION CONTRADICTS *TRINKO*.

The lower court's decision conflicts with *Trinko*. In *Trinko*, this Court held that when a monopolist has no antitrust duty to deal, there is no antitrust liability if the monopolist fails to provide "assistance in provision of service to rivals." *Trinko*, 540 U.S. at 410. As this Court explained:

> Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is ... some tension with the purpose of antitrust law,

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[4] *See also United States v. Trenton Potteries Co.*, 273 U.S. 392, 397 (1927) ("[t]he reasonable price fixed today may through economic and business changes become the unreasonable price of tomorrow"); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 283 (6th Cir. 1898) (stating that to inquire into the reasonableness of prices is to "set sail on a sea of doubt"), *aff'd* 175 U.S. 211 (1899).

[5] Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 ANTITRUST L.J. 841, 853 (1989).

> since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion.

Id. at 407-08. In the absence of an antitrust duty to deal, businesses need not provide favorable services or prices to their rivals.

There was no antitrust duty to deal here. The only reason the parties were transacting business at the upstream level was because of statutory compulsion. Federal law required the defendants to offer their DSL transport facilities to the plaintiffs. Therefore, the complaint here is predicated on a legal backdrop that is similar in one critical respect to that found in *Trinko*: parties that are dealing with each other under government compelled cooperation. *Id.* at 402. All that is left, post-*Trinko*, of the plaintiffs' price squeeze is a claim that the defendant's prices are too low in the downstream market. Absent predatory pricing, however, charging consumers low prices is of no concern to the antitrust laws.

Nor is this a case that falls within the "limited exception recognized in *Aspen Skiing*." *Trinko*, 540 U.S. at 409 (discussing *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 601 (1985)).

There is no allegation, required for recovery under an *Aspen Skiing* theory, that the defendant "voluntarily engaged in a course of dealing with its rivals, or would ever have done so absent statutory compulsion." *Trinko*, 540 U.S. at 409.

Moreover, as this Court has noted, "[a]ny claim for excessive rates can be couched as a claim for inadequate services and vice versa," *AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 223 (1998). Thus, the *Trinko* claim—inadequate service to rivals—logically can be characterized as a claim that excessive rates are being charged to rivals. Indeed, the D.C. Circuit recognized that the claims were the same. *Covad*, 398 F.3d at 673. Put another way, the *Trinko* claim is logically the same as a price-squeeze claim in this case. In both cases, a company that has no antitrust obligation to deal is being sued for an antitrust violation because it refuses to give favorable terms to a rival. Since the *Trinko* claim was invalid, then it logically follows that a price-squeeze claim also is invalid. *Covad*, 398 F.3d at 673-74.

The Ninth Circuit ignored this logic. Because *Trinko* did not specifically involve a price-squeeze claim, the court of appeals found that price claims "remain viable notwithstanding either the telecommunications statutes or *Trinko*." *Pet. App.* at 14. Under the Ninth Circuit's reasoning, a company that has no duty to deal cannot be sued for failing to assist its downstream competitors, *Trinko*, 540 U.S. at 410-11, but that same firm can be sued for failing to give favorable prices to its downstream

competitors. Such a distinction makes no sense. This Court should reaffirm *Trinko* and apply its holding to a price-squeeze claim.

CONCLUSION

For the reasons stated above, in the Brief of the Petitioners, and in the other amici briefs supporting the Petitioners, the decision of the Ninth Circuit should be **REVERSED**.

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AMICUS CURIAE BRIEF

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IN THE
Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
D/B/A AT&T CALIFORNIA, ET AL.,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AMICUS CURIAE COMPTEL IN SUPPORT OF RESPONDENTS

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INTEREST OF *AMICUS CURIAE*[1]

COMPTEL is the oldest and largest industry association representing competitive communications service providers and their supplier partners. COMPTEL members are entrepreneurial companies driving technological innovation and creating economic growth through competitive voice, video, and data offerings and the development and deployment of next-generation, IP-based networks and services. COMPTEL advances its members' interests through trade shows, networking, education, and policy advocacy before Congress, the Federal Communications Commission and the courts. COMPTEL works to ensure that competitive communications providers can continue to offer lower prices, better service, and greater innovation to consumers. As such, COMPTEL is acutely interested in how the antitrust laws apply in the communications industry. COMPTEL is also well-situated to supply this Court with information relevant to this case's resolution.

SUMMARY OF ARGUMENT

In the judgment under review, the court of appeals held that, even after this Court's decision in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), a

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[1] No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. Petitioners' blanket consent to the filing of amicus briefs is on file with the Clerk, and respondents' separate letter of consent is being filed together with this brief.

plaintiff states a claim under § 2 of the Sherman Act by alleging that the defendant engaged in a price squeeze – and did not require such a plaintiff to satisfy the predatory pricing standards of *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). Petitioners attack that holding, arguing that price squeezing should not be recognized as an independent tort under § 2. Respondents now agree with that position, stating that "it is clear respondents' pricing squeeze claim survives *Trinko* only if it satisfies the requirements of a predatory retail pricing claim under *Brooke Group*." Resp. Br. 13. Not only do respondents not seek to defend the judgment of the Ninth Circuit, but they embrace the *dissent* in that court. *Id.* at 18. Thus, with respect to the question presented – and the holding of the court of appeals – there remains no adversity between the parties, and this case has become moot. Any decision by this Court would be purely advisory, for regardless of how this Court resolves the question presented, respondents will not be proceeding on the legal theory it encompasses. Rather than issuing a precedential opinion on an important point of antitrust law, therefore, this Court should decline to address the merits of this case.

That course of action is what Article III of the Constitution requires. But it is also what prudence dictates, for the position that a price squeeze claim is viable as an independent antitrust tort – which respondents do not attempt to defend – in fact has ample support in law and policy. Federal courts have recognized price squeeze claims for more than

sixty years, with no sign of the parade of horribles that petitioners foretell. On the contrary, a firm's ability to bring a price squeeze claim prevents, deters, and can remedy multiple forms of anticompetitive harm – not to mention preventing circumvention of this Court's predatory pricing standards.

Nor is elimination of price squeeze claims justified by arguments that some price squeezes may not be anti-competitive or may be difficult for courts to adjudicate. Even if these arguments have merit in some instances, petitioners have not come close to justifying the complete abolishment of price squeeze claims. For instance, where upstream prices actually *exceed* downstream prices, or where the claim involves the juxtaposition of a weakly regulated upstream market with an unregulated downstream market, price squeezes can be both anti-competitive and amenable to straightforward judicial administration.

There is also no reason to conclude that this Court's decision in *Trinko* forecloses an independent price squeeze cause of action. *Trinko* addressed only the scope of a firm's antitrust duty to deal with rivals, and did not address the validity of price squeeze claims at all. Although the right not to deal with downstream competitors arguably encompasses a right not to deal with them at specific upstream prices, it logically cannot encompass a right to engage in *any* particular conduct in the downstream market – a necessary element of a price squeeze claim.

While respondents are content to pursue their price squeeze claim as a predatory pricing claim under *Brooke Group*, this Court should not require all price squeeze plaintiffs to satisfy that case's standards. The *Brooke Group* requirements, while not impossible for price squeeze victims to satisfy – indeed, the district court found they had been satisfied in this case – were designed for situations where the defendant's conduct consists entirely of price-cutting in the market in which the plaintiff seeks to compete. In a price squeeze, in contrast, the defendant's conduct *also* includes price increases in an upstream market in which the defendant possesses market power. In that context, it makes no sense to require a showing that the defendant's downstream prices were below its costs: The defendant can effectuate a price squeeze just as easily (and earn more profit without any corresponding benefit to consumers) by raising its upstream prices while keeping its downstream prices above cost. Nor does it make sense to require a showing of a dangerous probability of recoupment, since a price squeeze places less at risk for its perpetrator than does an ordinary predatory pricing scheme. In short, while some price squeeze victims may be able to satisfy *Brooke Group*, there would be no warrant for this Court to require *all* such victims to do the same.

Thus, there are strong reasons to preserve price squeeze claims as an independent cause of action under § 2 – yet as a result of respondents' concession and waiver, no concretely interested party is advancing these arguments. Both Article III and

prudence dictate that this Court should not rule on the merits of the question presented in the absence of adversarial presentation by a party with a concrete stake in the case.

ARGUMENT

I. BECAUSE THE PARTIES ARE NO LONGER ADVERSE AS TO THE QUESTION PRESENTED, THIS COURT SHOULD NOT ADDRESS THAT QUESTION'S MERITS

The court of appeals held that an antitrust plaintiff can state a § 2 claim by alleging that the defendant (an upstream monopolist) left insufficient margin between its upstream and downstream prices for the plaintiff to compete at the downstream level. In so holding, the court of appeals did not require such a plaintiff to satisfy the predatory pricing standards of *Brooke Group*. Petitioners challenge the court of appeals' holding, arguing that an allegation of a price squeeze is insufficient to state a claim under § 2. Respondents now agree on this important question of antitrust law: "it is clear," they state, that a price squeeze claim failing to meet the *Brooke Group* standards is not viable. Resp. Br. 13.[2] In fact, rather than defend the judgment of the court of appeals, respondents now agree with the approach

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[2] Petitioners appear to agree that a price squeeze claim that *does* satisfy the *Brooke Group* standards is viable. *See* Pet'rs' Br. 28 & n.17. And while the parties disagree on whether *respondents'* claim in fact satisfies *Brooke Group*, the court of appeals did not even address that question. In any event, neither of these interrelated questions is encompassed by the question presented.

advocated by the dissenting judge on the panel. *See id.* at 18.

Thus, petitioners and respondents agree that a plaintiff does not state a § 2 claim by alleging that the defendant "engaged in a 'price squeeze' by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete" – *i.e.*, that independent price squeeze causes of action do not survive *Trinko*. Pet'rs' Br. i (question presented). With both petitioners and respondents now aligned on that side of the question presented, *no party* with a concrete stake in this case's outcome is advocating for the contrary position. Yet the question presented involves an important and substantial point of antitrust law, one whose resolution would be imprudent in the absence of a genuinely adversarial airing of the issues.

In view of respondents' waiver and concession, therefore, the appropriate course is for this Court to refrain from deciding the question presented in a precedential manner. As this Court explained in *Deakins v. Monaghan*, 484 U.S. 193 (1988): "It is not enough that a controversy existed at the time the complaint was filed, and continued to exist when review was obtained in the Court of Appeals." *Id.* at 199. Rather, because respondents no longer disagree with petitioners on the question presented, that question has become moot. *See id.* ("first question on which certiorari was granted is moot" because "there no longer is a live controversy between the parties over" that question's resolution); *cf. Webster v. Reproductive Health Servs.*, 492 U.S. 490, 512-13

(1989) (controversy over particular statutory provision moot because of appellees' decision, on appeal, not to seek declaratory judgment with respect to that provision); *Williams v. Zbaraz*, 448 U.S. 358, 367-68 (1980) (vacating district court's decision of legal question that neither party raised, on ground that district court lacked jurisdiction to decide that question). No matter how this Court resolves the question presented, respondents will not litigate this case on the legal theory it encompasses. The lack of adversarial presentation by a concretely interested party makes it inappropriate for this Court to resolve the question presented. *See generally Flast v. Cohen*, 392 U.S. 83, 96-97 (1968) (discussing advisory opinions).

II. DECIDING THE QUESTION PRESENTED WOULD BE ILL ADVISED BECAUSE THERE ARE STRONG ARGUMENTS IN SUPPORT OF THE COURT OF APPEALS' DECISION

As explained above, the parties to this case now agree with each other that, after this Court's decision in *Trinko*, there is no basis for an independent price squeeze cause of action under § 2 of the Sherman Act. For that reason, this Court should not address the merits of the question presented. That approach is only reinforced by the fact that there are strong arguments – which respondents do not advance – in support of the viability of an independent price squeeze claim under § 2.

A. INDEPENDENT PRICE SQUEEZE CLAIMS UNDER § 2 ARE CONSISTENT WITH ANTITRUST LAW AND POLICY

1. Price Squeeze Claims Are Deeply Rooted In Antitrust Law

For more than half a century, federal courts have recognized price squeeze claims as a legitimate basis for recovery under § 2 of the Sherman Act. These courts have not found such claims difficult to administer or somehow inconsistent with general antitrust law principles. Nor, despite the lengthy pedigree of price squeeze liability, have petitioners pointed to instances where legitimate retail price cutting has been deterred by the prospect of price squeeze liability.

The price squeeze theory of recovery was first embraced by Judge Hand in *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) ("*Alcoa*"). In that case, the government charged Alcoa – the nation's only producer of aluminum ingot, from which aluminum sheet is made – with selling ingot at so high a price, and sheet at so low a price, that other sellers of sheet could not charge the same retail price and still make a profit. *Id.* at 437. Writing for the panel, Judge Hand explained that this conduct violated § 2 of the Sherman Act: "That it was unlawful to set the price of 'sheet' so low and hold the price of ingot so high, seems to us unquestionable, provided, as we have held, that on this record the price of ingot must be regarded as higher than a 'fair price.'" *Id.* at 438. As such, the price squeeze was "an unlawful exercise of

'Alcoa's' power after it had been put on notice by the 'sheet rollers' complaints." *Id.*; *see also George C. Frey Ready-Mixed Concrete, Inc. v. Pine Hill Concrete Mix Corp.*, 554 F.2d 551, 553 (2d Cir. 1977).

Since *Alcoa*, a long line of cases has confirmed that price squeeze claims provide a valid basis for antitrust recovery. Thus, for instance, in *Bonjorno v. Kaiser Aluminum & Chemical Corp.*, 752 F.2d 802 (3d Cir. 1984), the Third Circuit held that the defendant's deliberate manipulation of the relative prices of raw aluminum coil (the upstream product) and aluminum drainage pipe (the downstream product) gave rise to liability under § 2 on a price squeeze theory. *See id.* at 808-11. Likewise, in *City of Kirkwood v. Union Electric Co.*, 671 F.2d 1173 (8th Cir. 1982), the Eighth Circuit ruled that the district court should have considered the plaintiff's claim that the defendant's "wholesale rate increases . . . in conjunction with its smaller and deferred increases in retail rates [had] created a 'price squeeze.'" *Id.* at 1176; *see also id.* at 1176 n.4. In *City of Mishawaka v. American Electric Power Co.*, 616 F.2d 976 (7th Cir. 1980), the Seventh Circuit upheld the district court's imposition of price squeeze liability. *See id.* at 982-85.[3] And in *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992), while holding that there was no antitrust liability on the facts before the court, the Ninth Circuit explained that "[t]he vice that a price squeeze has is

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[3] *But cf. City of Mishawaka*, 616 F.2d at 984 (acknowledging that "the 'price squeeze' is only a part of the utility's conduct which as a whole was found to violate the Sherman Act").

that it can be used to cause severe damage to competitors by unjustifiably raising their costs of doing business." *Id.* at 1376. Indeed, a number of courts have recognized price squeeze claims even in regulated markets. *See City of Kirkwood*, 671 F.2d at 1179 (noting that neither the federal agency regulating wholesale rates nor the state agency regulating retail rates had "plenary authority over the interaction of wholesale and retail rates"); *City of Mishawaka*, 616 F.2d at 982-85.

Even *Town of Concord v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990) – on which petitioners heavily rely – did not categorically rule out antitrust liability for price squeezes. Far from it: in rejecting the claim before the court, then-Chief Judge Breyer emphasized that the court's reasoning "applies with full force only when the monopolist who engages in the squeeze is regulated at both industry levels," *id.* at 29, and then limited the court's holding to a subset of those circumstances. *Id.*; *see id.* at 28 (reasoning that "a price squeeze in a fully regulated industry . . . will not *normally* constitute 'exclusionary conduct' under Sherman Act § 2" (emphasis added)). Elaborating on the holding's limitation to monopolists "regulated at both industry levels," the court explained that "a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first." *Id.* at 29. And, despite noting the benefits that a vertically integrated monopolist could potentially provide to consumers, the court also detailed the economic

harms that can flow from a price squeeze. *See id.* at 23-24; *id.* at 25 (describing the harms and benefits of a price squeeze as "closely balanced").

2. Price Squeeze Claims Prevent Anti-Competitive Harm To Consumers

It is no wonder that courts of appeals have looked favorably on price-squeeze claims: vertically integrated monopolists can cause tangible and serious economic harms, especially when one of the markets in which they operate is unregulated. This threat to competition – not just to competitors, as petitioners maintain, Pet'rs' Br. 23 – counsels against eliminating an independent price squeeze cause of action under § 2.

First, price squeezes cause harm similar to that resulting from predatory pricing – a form of conduct that this Court has held is prohibited by § 2 of the Sherman Act. In *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), this Court recognized the dangers that arise when "[a] business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market." *Id.* at 222. *Brooke Group* imposed stringent requirements for a plaintiff to establish predatory pricing, however. Not only must the plaintiff show that the defendant's prices are below costs, but it also must show a "dangerous probability" that, in the long run, the defendant will be able to recoup these short-term losses by charging supracompetitive prices. *Id.* at 224. These stringent requirements reflect, in part,

this Court's assessment that "predatory pricing schemes are rarely tried, and even more rarely successful." *Id.* at 226 (quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589 (1986)). That is doubtless because predatory pricing schemes are highly speculative, posing the very real risk that low retail prices will result only in gains to consumers, not long-term benefit to the would-be monopolist. *See Matsushita*, 475 U.S. at 588-90.

Like a predatory pricing scheme, a price squeeze can squelch competition by effectively eliminating competitors' profit margins. But a price squeeze gives the monopolist a far greater possibility of financial reward than does predatory pricing. That is because, in a price squeeze, the upstream monopolist can reduce downstream competitors' profit margins not only by effectively reducing competitors' revenues (*i.e.*, lowering retail prices), but also by increasing their costs (*i.e.*, raising wholesale prices). And while the former tactic requires that the monopolist temporarily reduce its *own* revenues, the latter tactic may actually increase those revenues – or, at the very least, will reduce them less than would a retail-level price cut, because the monopolist can compensate for lost wholesale volume by selling the same products at the retail level. *See* IIIB Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 767c5, at 141 & n.15 (3d ed. 2008). Thus, an upstream monopolist seeking to engineer a price squeeze may risk less than a downstream monopolist seeking to implement a predatory pricing scheme. It stands to reason that price squeezes will therefore be attempted more

often than predatory pricing schemes, and will succeed more often.

At the same time, the cost of "false positives" in the price squeeze context is substantially less than it is for predatory pricing schemes. In *Brooke Group*, this Court stressed that low pricing might simply enhance consumer welfare, rather than reducing competition. *See* 509 U.S. at 223-24. But the same cannot be said of the wholesale side of a price squeeze, which entails *high* pricing. All other things remaining equal, increased wholesale prices will tend to reduce output at the upstream level (unless the current price is below the equilibrium price), and will tend to increase prices at the retail level. Neither of these is a consequence that courts should be anxious to preserve.

Second, and relatedly, price squeeze claims are necessary to prevent circumvention of *Brooke Group* by a downstream rival that has a monopoly on an upstream market. If a firm participates only in the downstream market, it can engage in exclusionary pricing only by lowering the downstream price. Eventually, that approach will run afoul of *Brooke Group*, as prices fall below costs. But if that same firm also has an upstream monopoly, it can stop short of lowering retail prices below costs, and raise upstream prices instead. That price-squeeze approach achieves the same result – anticompetitive reduction of rivals' profit margins – but does not risk liability under *Brooke Group*. Price squeeze liability under § 2 is therefore necessary to ensure that upstream monopolists are not able to execute an end-

run around *Brooke Group*'s safeguards against predatory pricing.

Third, price squeezes can create barriers to entry into the upstream and downstream markets. As then-Chief Judge Breyer recognized in *Town of Concord*, an upstream monopolist that uses a price squeeze to extend its monopoly power to a downstream market may thus deter new entrants in *both* markets. At the wholesale level, prospective entrants will fear that, having entrenched its power in the retail market, the monopolist will simply refuse to buy from them. Conversely, at the retail level, prospective entrants will fear that the vertically integrated monopolist will not allow them to purchase needed inputs (or will offer those inputs only on impracticable terms). Only reinforcing these fears is the fact that antitrust law ordinarily imposes no duty upon a monopolist to deal with competitors. *See Trinko*, 540 U.S. at 407-08. As such, "[t]he new firm might conclude that the only prudent way to challenge [the monopolist] would be to enter the industry at *both* levels at once. Insofar as it is more difficult for a firm to enter an industry at two levels than at one, the monopolist, by expanding its monopoly power, has made entry by new firms more difficult." *Town of Concord*, 915 F.2d at 23-24. And while petitioners argue (Pet'rs' Br. 24 n.13) that there was no allegation *in this case* that respondents intended to challenge petitioners' wholesale monopoly, that has no bearing on the validity of price squeeze claims as a general matter.

Fourth, allowing a vertically integrated monopolist to squeeze out competition in the downstream market can eradicate non-price competition. In the absence of downstream competition, that is, the monopolist has little incentive to improve its service or product. The result, of course, is harm to consumers. *See Town of Concord*, 915 F.2d at 24.

Petitioners nonetheless maintain that a price squeeze can have salutary effects, such as forcing less efficient competitors from the marketplace. *See* Pet'rs Br. 25-26. But the theoretical possibility of such effects in some circumstances does not counsel the blunderbuss approach of barring price squeeze claims altogether. It is, at most, merely a reason to scrutinize individual price squeeze claims, at later stages of litigation, to see if the practices at issue in fact give rise to the benefits that petitioners assert. And while petitioners and their amici make much of the prospect that potential price squeeze liability will chill legitimate retail price cutting, these predictions simply fail to grapple with the fact that price squeeze liability has been recognized for six decades without dire effects.

3. Price Squeeze Claims Are Particularly Meritorious In Certain Circumstances

Petitioners ask this Court to hold, categorically, that price squeezes are never independently actionable under § 2 of the Sherman Act. The harms outlined above amply demonstrate that this course of action would be ill-advised. But that is not all: as this case itself suggests, the facts of particular price

squeeze claims may bear on their viability and their consistency with antitrust law. Indeed, as discussed below, some price squeezes are particularly anticompetitive and reasonably easy for courts to address. That price squeeze claims can arise in a variety of factual contexts only confirms that this Court should not address the question presented, much less issue a broad ruling of any sort.

a. Price Squeeze Claims Can Be Especially Meritorious Where The Defendant's Upstream Price Exceeds Its Downstream Price

Petitioners argue that, because of the difficulty of determining an appropriate spread between a monopolist's upstream and downstream prices, price squeeze claims are unadministrable. *See, e.g.*, Pet'rs' Br. 30-33. But even assuming that *some* price squeeze claims are difficult to adjudicate for this reason, that is not the case where, as here, the monopolist's upstream price is actually *higher* than its downstream price – *i.e.*, where there is no spread at all.[4]

This Court's holding in *Brooke Group* provides a useful analogy. The *Brooke Group* Court was hesitant to give predatory pricing claims a broad

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[4] *See* J.A. 33. While there is some question whether the district court's order addressing the Amended Complaint was properly certified, even petitioners recognize that the Amended Complaint's "more detailed allegations can supply one version of facts that plaintiffs may posit in defending their claim by illustrating what they think they could have proved under the initial complaint." See Pet'rs' Br. 9 n.6.

reach because of a concern that predatory pricing may be "beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting." *Brooke Group*, 509 U.S. at 223. But the Court held that such claims *are* valid where a monopolist charges retail prices that are lower than its costs (assuming a dangerous probability of recoupment of the monopolist's short-term losses). *Id.* at 222-23. Similarly, it is conceivable that courts may have some difficulty adjudicating certain price squeeze claims. Yet where the monopolist's retail price is lower than the price it charges for the wholesale input, that pricing behavior is simply illogical, and its condemnation at the pleading stage requires no subjective assessment of whether the spread between the monopolist's retail and wholesale prices is somehow "too small."[5]

Indeed, determining whether the wholesale price exceeds the retail price is even easier than the inquiry that *Brooke Group* counsels for predatory pricing claims. For such claims, "[t]he difficulties of measuring costs are notorious." IIIA Areeda &

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[5] Opposing price-squeeze liability even in these circumstances, petitioners argue that "by providing Internet-access service, AT&T may acquire sources of revenue that supplement the retail service fee." Pet'rs' Br. 33 n.21. But while the potential for other sources of revenue might conceivably help the defendant prevail on the merits, it is far too speculative to require the plaintiff to negate this at the pleading stage. In any event, petitioners' argument about other sources of revenue proves too much: it implies that even below-cost retail pricing should not violate § 2 under *Brooke Group*, for the below-cost pricer "may acquire sources of revenue that supplement" the retail price.

Hovenkamp, *supra*, ¶ 740d, at 198; *see Brooke Group*, 509 U.S. at 222 n.1 (declining to resolve circuit court conflict over the appropriate measure of cost). In price squeeze claims, by contrast, the wholesale price the monopolist charges can easily be determined and "does not require judicial estimation of free-market forces." *Trinko*, 540 U.S. at 410 n.3; *see Town of Concord*, 915 F.2d at 28. For that reason, recognizing price squeeze claims where the wholesale price exceeds the retail price would be especially unlikely to deter legitimate retail price-cutting.

In fact, requiring that the wholesale price actually be lower than the retail price in order for a price squeeze claim to proceed is, if anything, too conservative: the wholesale price does not include the costs of any additional inputs added before a product is sold in the downstream market. In this case, for instance, the upstream input that petitioners sold to respondents was DSL transport, while the downstream product it sold to consumers comprised not only DSL transport, but also Internet access and certain additional amenities. Respondents have alleged that the wholesale price for DSL transport exceeded the price petitioners charged for the *entirety* of their retail product. J.A. 33. While this behavior surely demonstrates an "anti-competitive bent," *Trinko*, 540 U.S. at 409, the same would be true even if petitioners raised prices for their retail product – or lowered prices for wholesale DSL transport – to the point where the retail price equaled the sum of the wholesale DSL

transport price *and* the costs of the additional inputs included in the retail product.

b. Price Squeeze Claims Can Be Especially Meritorious Where They Involve Markets Regulated Only At The Upstream Level

As explained in greater detail below, *Trinko* heavily emphasized the pervasiveness of regulation in the relevant telephone markets, reasoning that antitrust enforcement would therefore have only minimal benefit. 540 U.S. at 412-13. Similar reasoning might conceivably apply to price squeeze claims: arguably, if both the upstream and the downstream markets are regulated, then in neither market will the monopolist have the incentive or ability to illegally acquire or maintain a monopoly. *See, e.g., Town of Concord*, 915 F.2d at 25-26.

In other cases, however, regulation may be limited to the upstream level. That distinction can be crucial. For where – as here – only the upstream market is regulated, the above logic does not hold. In such a scenario, an upstream monopolist may use a price squeeze to extend its monopoly into the unregulated retail market, where it can enjoy benefits of monopoly that would not be available if the retail market were regulated. The high rewards of executing a price squeeze in such a situation make it both particularly likely to occur (because of the monopolist's incentive to undertake the scheme) and particularly likely to cause anti-competitive harm.

In fact, where only the wholesale market is regulated, price squeezes arguably are more attractive to the upstream monopolist – and more likely to cause anti-competitive harm – than where there is no regulation at all. If neither the upstream nor the downstream market is regulated, then an upstream monopolist operating at the profit-maximizing level will not be able to gain any additional monopoly profit by obtaining market power downstream. *See, e.g.*, *Town of Concord*, 915 F.2d at 23. But when the upstream market is regulated, it is unlikely that the monopolist is gaining the entire monopoly profit, so it has an incentive to seek any uncaptured monopoly profit through other means.[6] One such means is monopolization of the unregulated downstream market. *See* IIIB Areeda & Hovenkamp, *supra*, ¶ 787b, at 354 (recognizing that where a regulated monopolist is "prevented by law from charging its profit-maximizing price in its primary market," vertical integration provides a means to "transfer . . . monopoly profits away from the regulated [upstream market], where the regulatory agency forbids the firm from charging its profit-maximizing price," to

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[6] While petitioners seek to rebut this possibility by noting that "respondents alleged that AT&T intends to make up for a reduction in margins *at the unregulated retail level* by charging more at the *regulated* wholesale level," Pet'rs' Br. 37; *see id.* at 28 n.17, that simply misapprehends the nature of the argument: it is only in the short term that a price-squeezing monopolist may seek to recoup lost retail profits at the wholesale level, while it is in the long term that the monopolist will seek to capture additional monopoly profits at the retail level.

the unregulated downstream market). While § 2 of the Sherman Act surely does not prohibit capturing monopoly profits as such, the opportunity to do so here makes it more likely that the monopolist will use anti-competitive behavior to seek a downstream monopoly.

Thus, the possibility of claims (such as respondents') arising from conduct in a market regulated only at the upstream level only confirms that this Court should not eliminate an independent price squeeze cause of action under § 2. *See Town of Concord*, 915 F.2d at 29 (noting "special problem" arising when monopolist regulated at one level seeks market power in a second, unregulated level).

c. Price Squeeze Claims Can Be Especially Meritorious Where Upstream Regulation Is Not Robust

Even in industries where one or both of the relevant markets is regulated, the relevant regulation may be lax, imperfect, or unable to prevent a predatory price squeeze. As this Court observed in *Trinko*, when "'[t]here is nothing built into the regulatory scheme which performs the antitrust function,' . . . the benefits of antitrust are worth its sometimes considerable disadvantages." *Trinko*, 540 U.S. at 412 (quoting *Silver v. New York Stock Exchange*, 373 U.S. 341, 358 (1963)) (first alteration in original).

Here, for instance, the regulation to which AT&T was subject was not – and is not – robust. Where ILECs provide DSL transport as a common carrier

service, as they were required to do at the time this case was initially brought, the Communications Act mandates that rates that be "just and reasonable," 47 U.S.C. § 201(b), and not "unreasonabl[y] discriminat[ory]," *id.* § 202(a). Neither the statute nor the FCC's interpretation thereof (as it stood at the time of the events underlying linkLine's Amended Complaint, *see infra* pp. 24-25 (discussing subsequent regulatory changes)) called for a comparison between the proposed upstream rate for DSL transport and the rate the ILEC charges for DSL-based Internet access.[7] Thus, regulation in this case would not have stopped an ILEC that was charging the maximum price for stand-alone DSL transport from lowering its retail price to that same level, erasing margins in that market and driving out its competitors while continuing to enjoy "a reasonable profit" on the wholesale side. And as long as the retail price was not below the ILEC's own costs, *Brooke Group* would prove no obstacle either.

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[7] It is far too speculative to say, as petitioners do, that "it has always been open to respondents to argue that AT&T's wholesale prices are unlawful in light of AT&T's retail prices." Pet'rs' Br. 36. *Federal Power Commission v. Conway Corp.*, which petitioners cite in support of this proposition, addressed only the jurisdiction of the Federal *Power* Commission to consider retail prices in its determination of whether wholesale prices were discriminatory – and, in reaching this conclusion, relied on specific provisions of the Federal Power Act. 426 U.S. 271, 277-79 (1976). In addition, that case made clear that the Commission lacked "power to remedy an alleged discriminatory or anticompetitive relationship between wholesale and retail rates by ordering the company to increase its retail rates." *Id.* at 276-77.

More generally, where regulation exists, "one must not leap from the premise of price regulation to the conclusion that the government is the effective price maker. Often the regulatory regime simply 'rubber stamps' the regulated firm's rate requests or inadequately supervises the rate determination process in other ways." IIIB Areeda & Hovenkamp, *supra*, ¶ 786, at 351 (footnote omitted). For instance, the measures of cost used by regulators "may give the public utility defendant too much leeway." *Id.*; *see City of Anaheim*, 955 F.2d at 1377 ("[B]ecause the regulatory systems do not work in perfect harmony, it is possibly for a utility to manipulate its filings and requests in a manner that causes a, at least temporary, squeeze which might be just as effective as one perpetrated by an unregulated actor."). These kinds of imperfections in the regulatory process can enable price squeezes to succeed in spite of regulation.

Indeed, a monopolist can use subtle means to increase its upstream prices without running afoul of regulators. For example, an ILEC can "account for costs so as to attribute some of them away from" the retail market and shift them towards the wholesale market. IIIB Areeda & Hovenkamp, *supra*, ¶ 787b, at 355. Doing so can artificially increase the ILEC's measure of "cost" for upstream rate-setting, thus facilitating one end of a price squeeze while

simultaneously concealing the fact that downstream prices are artificially low.[8]

d. Price Squeeze Claims Can Be Especially Meritorious Where Price Regulation Is Largely Absent

Beyond the possibility that price regulation may be lax, it may be essentially absent. That is, in fact, the current state of affairs for DSL. At the time of the events at issue in this lawsuit, ILECs providing DSL-based Internet service were required to offer DSL transport, on a nondiscriminatory basis, to non-facilities-based ISPs seeking to provide DSL-based Internet service. The rates at which ILECs provided DSL transport were closely supervised pursuant to the FCC's tariffing regime. See Pet'rs' Br. 3-4. But that regulatory landscape has since changed dramatically. Specifically, in the wake of this Court's decision in *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967 (2005), the FCC ruled that, subject to a one-year transition period, "all wireline broadband Internet access service providers are no

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[8] In addition, even where an upstream monopolist is required to use a separate subsidiary to provide the downstream product, nondiscrimination requirements may pose little impediment to a price squeeze. To be sure, high upstream prices, coupled with low downstream ones, may mean that the subsidiary will not itself turn a profit. But the subsidiary's bottom line will be deceiving, because per-unit losses attributable to high upstream prices will, by definition, be offset by gains to the upstream parent. Thus, prohibitions on price discrimination may not prevent a price squeeze from occurring.

longer subject to the . . . requirement to separate out the underlying transmission from wireline broadband Internet access service and offer it on a common carrier basis." Report and Order and Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, 20 FCC Rcd 14,853, ¶ 41 (2005) ("*2005 Broadband Order*"), *petition for review denied, Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205 (3d Cir. 2007). Instead, wireline broadband Internet access service providers may "choose to offer the transmission component of wireline broadband Internet access services to both affiliated and unaffiliated ISPs or others on a non-common carrier basis or a common carrier basis." *Id.* ¶ 86. And, "to the extent they choose to offer that transmission as common carriage, they may do so either under tariff or on a non-tariffed basis." *Id.* ¶ 94. While minimal regulation does remain, it does not impose an obligation to sell DSL transport to ISPs, nor does it place significant restrictions on the price that can be charged for such service.[9] *See, e.g., id.* ¶ 6.

In the absence of substantial regulation even at the upstream level, there simply is no basis on which

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[9] Although AT&T itself, as a condition of a recent merger, is currently obligated to offer DSL transport at a price no higher than the rate it charges for retail DSL-based Internet service, *see* Pet'rs' Br. 4-5 n.4, that obligation does not extend to the industry as a whole – and, moreover, is itself a "voluntary commitment[]" offered by AT&T and its partner in the merger. *See* Memorandum Opinion and Order, *AT&T Inc. & BellSouth Corp. Application for Transfer of Control*, 22 FCC Rcd 5662, 5807, 5814, *on partial reconsideration on other grounds*, 22 FCC Rcd 6285 (2007).

to conclude that suits by private plaintiffs under § 2 are unnecessary or superfluous. Not only will a monopolist face no impediment to charging high upstream prices in the course of executing a price squeeze, but it also will face no impediment to charging high downstream prices after forcing out competition.[10] The lack of regulation thus counsels strongly against the abolition of price squeeze claims. Moreover, as the DSL example demonstrates, a regulated industry may not remain so – a fact that may spur even a regulated monopolist to undertake a price squeeze in anticipation of future deregulation.

Thus, there are strong arguments in support of the viability of an independent price squeeze claim under § 2, which are not advanced (much less fully briefed on a developed record) by any party to this case. This provides a further reason for this Court not to address the merits of the question presented.

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[10] As with the FCC's longstanding practice of not regulating retail prices of DSL-based Internet access, it cannot be argued that the lack of current upstream regulation represents an exercise of regulatory authority with which the antitrust laws should not interfere. *See* Amicus Br. of Verizon Commc'ns 30-31. That is because the FCC's 2005 order rested principally on its determination that facilities-based wireline broadband Internet access service is not (and does not include) a "telecommunications service," and thus is outside the FCC's Title II jurisdiction. *2005 Broadband Order* ¶¶ 5, 12-17, 102-107. Moreover, aside from rare instances where a carrier *chooses* to offer DSL transport as a "telecommunications service" on a common-carrier basis, *see id.* ¶¶ 86, 89-90, any upstream regulatory authority that the FCC continues to assert is grounded only in the FCC's so-called Title I "ancillary jurisdiction," *see id.* ¶¶ 108-110 – a concept whose breadth is not entirely settled.

B. NEITHER *TRINKO* NOR *BROOKE GROUP* WOULD CONTROL THE RESOLUTION OF THE QUESTION PRESENTED

To bolster their sweeping attack on all price squeeze claims, petitioners and their amici rely heavily on two of this Court's decisions: *Trinko* and *Brooke Group*. Specifically, they contend that *Trinko* eliminates the possibility of an independent price squeeze cause of action. And, having reached that conclusion, they maintain that victims of a price squeeze should simply have their claims tested against the predatory pricing standards articulated by *Brooke Group*. *See, e.g.*, Gov't Br. 15-18; *see also* Pet'rs' Br. 28 & n.17. Respondents now agree with these contentions – but this Court should not embrace them, for the arguments to the contrary are strong indeed.

1. Trinko *Does Not Compel A Ruling For Petitioners*

Petitioners assert that a result in their favor follows ineluctably from this Court's decision in *Trinko*. Likewise, respondents believe that *Trinko* forecloses price squeeze claims under § 2 that do not satisfy the *Brooke Group* standards. Resp. Br. 13. Both petitioners and respondents are mistaken. *Trinko* does not say anything about the viability of price squeeze claims, and it certainly does not say anything about the viability of the price squeeze claim in *this* case.

In *Trinko*, this Court considered whether an incumbent local exchange carrier (ILEC) had

violated § 2 of the Sherman Act by "den[ying] interconnection services to rivals" seeking to compete in the local telephone market, where the 1996 Telecommunications Act had required the ILEC to provide rivals with those services. *Trinko*, 540 U.S. at 407. Interpreting this allegation as a claim of "refusal to deal," the Court first reaffirmed that such a claim generally is not viable under § 2. *See id.* at 408-09. It then reasoned that the particular refusal-to-deal claim before it did not pass muster. *See, e.g., id.* at 410 ("We conclude that Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents.").

Trinko thus limited itself to the viability of a claim of refusal to deal. It plainly did not address the viability of a price squeeze claim – nor could it have done so, because the respondent pressed no such claim. *See Covad Commc'ns Co. v. BellSouth Corp.*, 374 F.3d 1044, 1050 (11th Cir. 2004) (noting that "[t]he plaintiffs' amended complaint in *Trinko* did not state any price squeezing claims"); *compare* Pet'rs' Br. 17 (maintaining that "[t]he factual allegations of respondents' complaint and the complaint in *Trinko* are indistinguishable"). And a reluctance to recognize refusal-to-deal claims certainly does not imply a corresponding reluctance to recognize price squeeze claims. In fact, this Court cited nearly century-old precedent in support of its conclusion that there is generally no duty to deal, creating a glaring contrast with the fact that, as discussed above, courts have long considered price squeeze claims viable under § 2. *See Trinko*, 540

U.S. at 408 (citing *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)). If price squeeze claims truly were inconsistent with "the long recognized right of [a] trader or manufacturer . . . freely to exercise his own independent discretion as to parties with whom he will deal," *id.* (quoting *Colgate*, 250 U.S. at 307) (first alteration in original), courts would have long since rejected *Alcoa*.

Nonetheless, petitioners vigorously argue that the absence of a duty to deal with rivals implies the absence of a duty not to effect a price squeeze. Pet'rs' Br. 15-16. Yet that reasoning reflects a misreading of *Trinko*. In *Trinko*, this Court treated Verizon's "deni[al of] interconnection services to rivals" as a "refusal to deal," arguably implying that without an antitrust duty to deal with its rivals in the first place, a firm generally can deal with them on whatever terms it wishes. *See* 540 U.S. at 407-09. In arguing that price squeezes therefore are permissible under *Trinko*, petitioners essentially contend that a price squeeze claim – like the claim at issue in *Trinko* – rests on an asserted duty to deal with rivals on particular terms. That is incorrect. The nub of a price squeeze claim is not just that the monopolist has charged high upstream prices to its rivals, but that it has made it impossible for rivals to compete by choosing a particular combination of upstream *and downstream* prices, the latter charged not to downstream *rivals* but to downstream *customers*. A price squeeze thus is not a species of

refusal to deal with rivals on particular terms and, accordingly, does not fall within *Trinko*'s scope.[11]

Further, petitioners' argument ultimately rests on the notion that the greater must include the lesser. Setting aside the fact that a price squeeze simply is not "lesser" than a refusal to deal with rivals (as set forth above), we note that this Court has not hesitated to reject "greater includes the lesser" arguments in the past. *See, e.g.*, *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 510-11 (1996); *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 836-37 (1987); *see also* Richard A. Givens, *Antitrust: An Economic Approach*, § 13.01, at 13-7 (2008) ("The concept that the greater includes the lesser . . . does not necessarily follow in antitrust law, any more than similar arguments are always accepted in the constitutional field." (footnote omitted)).[12]

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[11] Moreover, in light of the FCC's 2005 order, it is clear that, as a general matter, ILECs currently selling DSL transport to non-facilities-based ISPs are dealing with them voluntarily. *But cf.* note 9 supra. And, as *Trinko* made clear, a course of prior voluntary dealing is a reason for permitting some refusal-to-deal claims. 540 U.S. at 409. To the extent that *Trinko*'s "no duty to deal" reasoning provides a basis for rejecting some price squeeze claims (which it does not), that reasoning has no application to price squeeze claims arising out of conduct taking place after the 2005 order became effective.

[12] As to this particular case, moreover, *Trinko* would be distinguishable because of respondents' allegations that petitioners' upstream prices exceeded their downstream prices. In reaffirming that there generally is no antitrust duty to deal with competitors, *Trinko* noted that the ILEC in question had

2. *A Successful Price Squeeze Claim Need Not Allege The Elements Of A Predatory Pricing Claim Under* Brooke Group

In urging this Court to reject all independent price-squeeze claims, petitioners and their amici advocate a regime (as do respondents) under which, for victims of a price squeeze, *Brooke Group* is the only game in town. *See, e.g.*, Gov't Br. 15-18; Resp. Br. 13; *see also* Pet'rs' Br. 28 & n.17. This Court held in *Brooke Group* that a successful predatory pricing claim must allege (a) below-cost retail pricing; and (b) a "dangerous probability" that the defendant will recoup short-run losses by later charging supracompetitive prices. 509 U.S. at 224. As respondents amply explain, a price squeeze claim that satisfies these standards surely should survive. But contrary to petitioners' contentions, it would be inappropriate to *require* a price-squeeze victim to allege (or prove) the elements set forth by *Brooke Group*.

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refused to deal with competitors "at the cost-based rate of compensation available under [the 1996 Telecommunications Act]." 540 U.S. at 409. It thus distinguished *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), an earlier case finding a duty to deal, on the ground that the *Aspen Skiing* defendant had "revealed a distinctly anticompetitive bent" by refusing to sell to a competitor "*even if compensated at retail price*." *Trinko*, 540 U.S. at 409 (emphasis in original); *see id.* (noting that these facts "suggest[ed] a calculation that its future monopoly retail price would be higher"). *Id.* In this case, petitioners' upstream prices in excess of their downstream prices necessarily imply a refusal – as in *Aspen Skiing*, and in contrast with *Trinko* – to deal with respondents at retail price.

First, it would make little sense to require a price-squeeze victim to allege that the defendant priced its retail products below cost. In imposing that requirement on a predatory-pricing plaintiff, *Brooke Group* stressed that "[l]ow prices benefit consumers regardless of how those prices are set." *Id.* at 223 (quoting *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990)). Yet a price squeeze consists not only of low downstream pricing, but also of high upstream pricing – and the latter simply cannot be said to benefit consumers or otherwise promote competition. Indeed, as explained above, one danger of a price squeeze is that it can enable an upstream monopolist to circumvent *Brooke Group* by stopping short of below-cost downstream pricing, and increasing its upstream pricing instead. In short, requiring a price squeeze victim to allege below-cost pricing would improperly ignore the other side of the price squeeze vise.

Second, it would make equally little sense to require a price squeeze victim to show a dangerous probability of recoupment. *Brooke Group* imposed this requirement because "[w]ithout [recoupment], predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced," 509 U.S. at 224; *see id.* (explaining that "unsuccessful predation is in general a boon to consumers"). But a price squeeze, unlike a predatory pricing scheme, does not necessarily "produce[] lower aggregate prices in the market" in the short term. *Id.* That is because the upstream side of a price squeeze consists of *increased* prices (and potentially reduced output). Indeed, while a predatory pricing scheme necessarily

requires the perpetrator to sacrifice short-term profits – with no guarantee of offsetting returns in the long run – a price squeeze may entail no short-term sacrifice of profits at all, depending on the effect of increased upstream prices on upstream revenues. At a minimum, as explained above, a price squeeze is likely to place less at risk for the upstream monopolist than is an ordinary predatory pricing scheme. It therefore would be improper to require a price squeeze victim to make the *Brooke Group* showing of a dangerous probability of recoupment.

* * *

None of this is to suggest that this case is a proper vehicle for this Court to affirm the validity of price squeeze claims under § 2 of the Sherman Act, or otherwise to issue any ruling on the question presented. Rather, it is only to show that there are strong arguments in support of the Ninth Circuit's decision – arguments that could be fully aired only if respondents, not just an amicus curiae, sought to defend that decision. But respondents now concede that decision was wrong, and they will not proceed with an independent price squeeze claim regardless of the answer to the question presented. As a result of that concession, no party with a concrete stake in this case stands ready to defend the validity of independent price squeeze claims under § 2. As to the important point of antitrust law on which this Court granted certiorari, this case is now moot, and resolution of the question presented should therefore be left for another day.

CONCLUSION

This Court should not reach the merits of the question presented.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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IN THE

Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY
d/b/a AT&T CALIFORNIA, *et al.*,

Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,

Respondents.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF OF *AMICI CURIAE* PROFESSORS AND SCHOLARS IN LAW AND ECONOMICS IN SUPPORT OF THE PETITIONERS

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SEW A

QUESTION PRESENTED

Whether a plaintiff states a claim under section 2 of the Sherman Act by alleging that the defendant—a vertically integrated retail competitor with an alleged monopoly at the wholesale level but no antitrust duty to provide the wholesale input to competitors—engaged in a "price squeeze" by leaving insufficient margin between wholesale and retail prices to allow the plaintiff to compete.

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No. 07-512

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BRIEF OF *AMICI CURIAE* PROFESSORS AND SCHOLARS IN LAW AND ECONOMICS IN SUPPORT OF THE PETITIONERS

INTERESTS OF THE *AMICI CURIAE*[1]

Amici are professors and scholars in law and economics who have taught, or have conducted research

1. No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than Amici Curiae, or their counsel, made a monetary contribution to its preparation or submission. The parties have consented to the filing of this brief and such consents are being lodged herewith.

on, antitrust law and the economics of industrial organization. They include William J. Baumol, Robert H. Bork, Robert W. Crandall, George Daly, Harold Demsetz, Jeffrey A. Eisenach, Kenneth G. Elzinga, Richard A. Epstein, Gerald Faulhaber, Franklin M. Fisher, Charles J. Goetz, Robert Hahn, Jerry A. Hausman, Keith N. Hylton, Thomas M. Jorde, Robert E. Litan, Paul W. MacAvoy, Sam Peltzman, J. Gregory Sidak, Pablo T. Spiller, and Daniel F. Spulber. A summary of names and affiliations appears in the Appendix at the end of this brief. *Amici* file solely as individuals and not on behalf of any institutions with which they are affiliated.

INTRODUCTION

As professors and scholars in law and economics who teach and conduct academic research on antitrust law, we agree with the petitioners that the Ninth Circuit has generated an inescapable conflict among circuits, and that the Ninth Circuit's opinion below is incompatible with this Court's reasoning in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069 (2007), and *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). We agree with Judge Gould's dissent in *linkLine* that *Trinko* "takes the issues of wholesale pricing out of the case," such that the plaintiffs' only possible remaining theory of harm would be predatory pricing at the retail level—which the plaintiffs did not allege. *linkLine Commc'ns Inc. v. Pac. Bell Tel. Co. d/b/a/ AT&T Cal., Inc.*, 503 F.3d 867, 886

(9th Cir. Sept. 11, 2007) (Gould, J., dissenting). We also agree with Judge Ginsburg's opinion for the D.C. Circuit in *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005), which in turn embraces the conclusion of the Areeda-Hovenkamp treatise that "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Id.* at 673-74 (quoting 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 767c3, at 129-30 (2d ed. 2002)). The existence of a rule like *linkLine* has a pervasive impact on business behavior that, at the margin, affects competition and consumers. This deleterious effect extends beyond the telecommunications industry to affect all firms that do business in the Ninth Circuit.

SUMMARY

In our minds, an even larger issue is at stake in this case. The Ninth Circuit's decision in *linkLine* implicates the normative foundation of modern Sherman Act jurisprudence: that antitrust law exists to advance consumer welfare. We have three points to make.

First, any rule of price-squeeze liability that threatens liability based on the claim that the difference between a firm's upstream and downstream prices leaves downstream rivals insufficient margin substitutes a rule of competitor welfare for consumer welfare.

Second, properly understood, a price squeeze is a regulatory issue, which makes sense only as a rule of price regulation in an industry already subject to duties to deal and to control by institutionally competent

regulators. Attempting to implement regulatory policy through section 2 of the Sherman Act is ill-advised, both because it makes no sense for courts to re-regulate deregulated or lightly regulated industries, and because courts lack the institutional competence to implement regulation.

Third, the Ninth Circuit's rule is of pressing concern precisely because it will deter efficiency-enhancing conduct and competitive pricing. Vertical integration and partial integration are ubiquitous, and firms need to be able to make decisions about such integration without the threat of liability. Vertically integrated firms likewise need to be free to cut retail prices (as long as the prices are not predatory) without concern for rivals—the point of *Brooke Group*. Moreover, the Ninth Circuit's standard is so vague and open-ended that it creates uncertainty and invites litigation; it also permits imposition of liability based on apparently subjective evaluation of disputed and hard-to-prove facts, which will lead to a substantial risk of false positives.

ARGUMENT

It is not possible to advance consumer welfare with an antitrust rule that punishes a firm for failing to ensure its competitors' profitability. If *linkLine* stands, the lower federal courts will have put antitrust at war with itself to a degree not witnessed since the years before the Court's conscious decision, three decades or more ago, to infuse antitrust law with greater economic rigor so that it might better advance consumer welfare.

The alternative to consumer-welfare maximization is the view that antitrust law is simply one more tool of industrial policy, and thus its application may permissibly compromise consumer welfare to advance the welfare of competitors. Other nations evidently consider this normative proposition to be appropriate, if recent developments in the European Union are a valid indication. More than ever before, the United States and Europe appear to be at a fork in the road over whether the law of monopolization exists to protect consumers or to ensure that a specified number of firms will profitably populate a market. The Ninth Circuit's *linkLine* decision implicitly chooses the latter path, which leads to the Potemkin village of "managed competition." *See* Robert W. Crandall & Hal J. Singer, *Life Support for Unaffiliated ISPs?*, REGULATION, Fall 2005, at 46. *See also* Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct?*, 4 J. COMPETITION L. & ECON. 271 (2008); J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 J. COMPETITION L. & ECON. 279 (2008).

To say that American antitrust law does not—and should not—recognize a cause of action for price squeeze by a firm that owes no duty to deal with rivals is not to say that one cannot find the concept of a price squeeze embraced somewhere else in American law. One can. In public utility regulation, the price-squeeze issue arises in proceedings concerning "access pricing" and "imputation."[2] Extensive economic literature exists on

2. *See, e.g.*, WILLIAM J. BAUMOL & J. GREGORY SIDAK, TOWARD COMPETITION IN LOCAL TELEPHONY (MIT Press 1994); William J. (Cont'd)

how regulators would maximize consumer welfare in the pricing of bottleneck inputs that a vertically integrated monopolist sells to its competitors in a downstream market. But three points about price-squeeze regulation bear emphasis.

First, these cases are highly technical *regulatory* proceedings that are typically protracted and factually intensive. *See Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, J.) (a price-squeeze case requires a court to "act[] like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years"). Price-squeeze cases are precisely the kinds of proceedings that would be unwieldy to attempt to replicate through antitrust litigation. Imputation analysis requires the estimation of incremental cost. Economic estimation of that nature demands a kind of quantitative expertise that a judge or jury is not likely to possess. Even so ambitious and invasive a monopolization case as the Bell System divestiture, *United States v. AT&T Corp.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom.* Maryland v. United States, 460 U.S. 1001 (1983), did not attempt to use antitrust law as a tool for regulating the price of wholesale services supplied by monopoly local exchange carriers.

(Cont'd)

Baumol & J. Gregory Sidak, *The Pricing of Inputs Sold to Competitors*, 11 YALE J. ON REG. 171 (1994); William J. Baumol & J. Gregory Sidak, *The Pricing of Inputs Sold to Competitors: Rejoinder and Epilogue*, 12 YALE J. ON REG. 177 (1995); Jerry A. Hausman & Timothy J. Tardiff, *Efficient Local Exchange Competition*, 40 ANTITRUST BULL. 529 (1995).

Second, these regulatory proceedings arise because the vertically integrated firm has a preexisting regulatory duty to deal with competitors in a downstream market. This feature is the element of compulsion that was so critical to the Court's reasoning in *Trinko*. *See Trinko*, 540 U.S. at 412-16.

Third, the experience with price-squeeze cases brought by national competition authorities in Europe under Article 82 of the Treaty of Rome reveals the economic and factual complexity of correctly implementing the imputation analysis in an antitrust case. It becomes necessary to hypothesize what an efficient competitor would be and then determine whether the defendant's wholesale and retail prices permit the efficient competitor to earn some level of profit deemed to be sufficient.[3] This kind of analysis, however, merely underscores (1) that the primary concern in price-squeeze cases is not consumers, but competitors, and (2) that, in the American setting, the requisite analysis more resembles the work of a public utilities commission than that of a federal judge presiding over an antitrust case. By definition, the judge's job as de facto rate regulator never ends because external forces will compel wholesale and retail prices to change over time, such that a given profit margin

3. *See, e.g.*, Michele Polo, *Price Squeeze: Lessons from the* Telecom Italia *Case*, 3 J. COMPETITION L. & ECON. 453 (2007); Laura Ferrari Bravo & Paolo Siciliani, *Exclusionary Pricing and Consumer Harm: The European Commission's Practice in the DSL Market*, 3 J. COMPETITION L. & ECON. 243 (2007); Damien Geradin & Robert O'Donoghue, *The Concurrent Application of Competition Law and Regulation: The Case of Margin Squeeze Abuses in the Telecommunications Sector*, 1 J. COMPETITION L. & ECON. 355 (2005).

may shrink and jeopardize the survival of competitors. The perverse outcome is that price-squeeze litigation becomes a kind of enduring cost-of-service regulation that taxes the resources of a single district judge.

The Telecommunications Act of 1996 provides an instructive analogy that provoked multiple opinions in *AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366 (1999). There, the statute (applied in a regulatory proceeding) entitled a competitor to access any one or more of an incumbent local exchange carrier's unbundled network elements at a regulated price if that competitor would be "impaired" in its ability to supply a (downstream) telecommunications service in the event that the competitor were denied access to a particular network element (at the regulated price). Congress did not attempt to provide a precise economic definition of "impairment." It is a measure of the complexity of administering that concept that Justices Scalia, Breyer, and Souter debated how much of a cost disadvantage would be enough to trigger the "impairment" standard. *Iowa Util. Bd.*, 525 U.S. at 392, 399-400, 416-18. That question admitted no easy answer—and it got none in multiple remands to the Federal Communications Commission over the course of many years. Yet the determination of "impairment" under the Telecommunications Act fundamentally resembles the line of economic analysis that a court would need to undertake in a price-squeeze case based on the Sherman Act.

Shortly after *Iowa Utilities Board*, some scholars on telecommunications regulation argued that the "impairment" exercise should be regarded as

unproductive unless it could be shown that finding "impairment" and granting a competitor access to the incumbent's bottleneck element at a regulated price would increase consumer welfare in the downstream market. *See* Jerry A. Hausman & J. Gregory Sidak, *A Consumer-Welfare Approach to Mandatory Unbundling of Telecommunications Networks*, 109 YALE L.J. 417 (1999). In other words, if there is no causal connection between assisting competitors and improving consumer welfare, then the regulatory intervention is strictly a wealth transfer. The same criticism applies to an antitrust cause of action for price squeeze. The theory of price squeeze is dissonant with consumer welfare maximization for the simple but perverse reason that, as conceived by the Ninth Circuit, harm to consumer welfare is irrelevant to the imposition of antitrust liability.

A word about *United States v. Aluminum Co. of America (Alcoa)*, 148 F.2d 416 (2d Cir. 1945), is necessary because the Ninth Circuit is incorrect to the extent that it reads *Alcoa* to have imposed section 2 liability under a price-squeeze theory for an attempt to monopolize the downstream (aluminum sheet) market. It is too abbreviated for the Ninth Circuit to characterize *Alcoa* as "holding [Alcoa's] price squeeze unlawful," *linkLine*, 503 F.3d at 880, and then to assert that "a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*. . . ." *Id.* at 883.

In *linkLine*, the plaintiffs argued that the telephone company used its retail pricing of broadband Internet access (aluminum sheet) and its pricing of DSL transport (aluminum ingot) to monopolize broadband

Internet access (aluminum sheet). In *Alcoa*, however, the Second Circuit said that the price squeeze, which it found to deny downstream competitors a "living profit" in violation of section 2 of the Sherman Act, "was not part of an attempt to monopolize the 'sheet' market." *Alcoa*, 148 F.2d at 438. Because the analogy to sheet aluminum in *linkLine* is broadband Internet access (not DSL transport), *Alcoa* does not support the position of either the plaintiffs or the Ninth Circuit that the alleged price squeeze potentially violates section 2 *with respect to the market for broadband Internet access.*

Moreover, *Alcoa*'s concern over preserving a "living profit" for Alcoa's competitors could not be farther removed from the contemporary consumer-welfare orientation of antitrust law. The Court in *Trinko* considered *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), to be on the ragged edge of viability as a theory of antitrust liability. The "living profit" reasoning of *Alcoa* should be sufficient to confirm that, sometime during the intervening 62 years, the Court's evolving jurisprudence based on consumer-welfare maximization implicitly overruled the competitor-welfare premise of *Alcoa*'s price-squeeze analysis.[4] For example, in *Trinko* this Court said that courts should not act as "central planners." *Trinko*, 540 U.S. at 408. However, to determine a "fair price" and a

4. Compare, for example, how the D.C. Circuit in *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 226 (D.C. Cir. 1986) (Bork, J.), reasoned that, by 1986, certain Supreme Court decisions had been implicitly overruled by the analysis contained in the Court's more recent cases embracing the consumer-welfare approach.

"living profit," two of three elements of a prima facie price-squeeze claim under the *Alcoa* analysis, a court must do just that. Forcing a firm to share its resources with downstream competitors, and dictating "fair prices" for these resources, strains the resources of the judiciary, as this Court has noted.

In *Alcoa*, the Second Circuit asserted that the purpose of the Sherman Act is to "preserve, for its own sake and *in spite of possible cost*, an organization of industry in small units." *Alcoa*, 148 F.2d at 429 (emphasis added). All of the legal analysis in *Alcoa* that builds from this premise is suspect in light of the fact that, at least three decades ago, this Court emphatically expressed a different normative objective for antitrust law. Today, *Alcoa*'s view of the normative purpose of antitrust law more closely resembles Europe's perspective than America's. In *NCAA v. Board of Regents of the University of Oklahoma*, 468 U.S. 85 (1984), *Trinko*, and many other cases, this Court has endorsed the view that the Sherman Act's concern is consumer welfare, not competitor welfare. Compelling an income transfer from a vertically integrated firm to its downstream competitors does not advance the Sherman Act's consumer-welfare goal.

In light of this weak foundation for the price-squeeze theory of liability, we find it startling that the Ninth Circuit never discussed the First Circuit's decision in *Town of Concord*, written in 1990 by then-Judge Breyer. *Town of Concord* is the single most informative opinion in American antitrust jurisprudence for understanding the law and economics relevant to evaluating a price-squeeze claim. It is no surprise that this Court's decision

in *Trinko* quotes liberally from *Town of Concord* and confirms the correctness of its reasoning that the antitrust laws are concerned with the competitive *process*, not its end results. The Ninth Circuit relied on decisions from the Second, Third, Seventh, and Eighth Circuits—but its survey of the pertinent law on price squeezes did not reach Judge Breyer's extended analysis in *Town of Concord*.

In *Town of Concord*, the First Circuit rejected a price-squeeze claim for reasons that implicate the validity of *Alcoa*. First, the court noted that a price squeeze can have procompetitive effects: "the primary-level monopolist might carry out its second-level activities more efficiently than its independent competitors," thereby eliminating less efficient second-level competitors from the market, which results in lower prices and saves economic resources. 915 F.2d at 24. Moreover, if a second-level firm is itself a monopolist, it is desirable to allow the upstream monopolist to squeeze out the downstream monopolist, because the downstream monopolist, in its effort to extract its own monopoly rents, can increase the price of the end-product beyond the price that results from just one firm's extraction of monopoly rent (either realized at the wholesale or retail level). *Id.* at 24-25. For this reason, antitrust scholars applaud the elimination of this phenomenon of "double marginalization." *See, e.g.*, 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 758b at 30 (2d ed. 2002).

Second, foreshadowing the Supreme Court's concerns in *Trinko*, Judge Breyer highlighted the adverse administrative considerations that counsel

against recognizing price-squeeze claims. These administrative considerations implicate *Alcoa*'s core elements: a "fair price" for the wholesale product and a "living profit" for second-level competitors. Questioning the practicality of administering remedies for an unlawful price squeeze, Judge Breyer asked rhetorically how a judge or jury could determine a fair price or a proper price gap between the wholesale and retail prices. *Town of Concord*, 915 F.2d at 25. What *Trinko* recognized as a fatal flaw in a refusal-to-deal theory—namely, that "[e]nforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited," *Trinko*, 540 U.S. at 408—is, as *Town of Concord* indicates, just as fatal for an *Alcoa* price-squeeze claim. As explained by the current chief economist of the Antitrust Division of the Department of Justice, to determine a "fair price" or a "living profit" for firms that meet some threshold level of efficiency, courts must "become a type of regulatory body setting complex terms . . . in an area where, unlike a regulatory body, the courts have no special expertise." Dennis W. Carlton, *A General Analysis of Exclusionary Conduct and Refusal to Deal—Why* Aspen Skiing *and* Kodak *Are Misguided*, 68 ANTITRUST L.J. 659, 662 (2001).

CONCLUSION

In sum, it is imperative that the Court clarify that the price-squeeze theory is a regulatory undertaking, not an antitrust cause of action. It is neither feasible nor advisable to use antitrust law to make a vertically integrated firm responsible for ensuring the profitability of its competitors in the downstream market. Such a rule would create a powerful incentive for the vertically integrated firm to raise its retail price to reduce the risk of antitrust lawsuits by unprofitable downstream competitors. That result is antithetical to the consumer-welfare objective that animates American antitrust law.

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AMICUS CURIAE BRIEF

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PACIFIC BELL TELEPHONE COMPANY, DBA AT&T CALIFORNIA, *et al.*,
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR VERIZON COMMUNICATIONS INC. AND THE NATIONAL ASSOCIATION OF MANUFACTURERS AS *AMICI CURIAE* SUPPORTING PETITIONERS

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INTEREST OF *AMICI CURIAE* [1]

The businesses owned by Verizon Communications Inc. (Verizon), like those of AT&T, provide wireless and wireline communications services directly to retail customers and, on a wholesale basis, to other communications service providers that compete with Verizon at the retail level. In particular, Verizon is competing at both retail and wholesale for broadband services that provide high-speed connections to the Internet.

The truly important advances on the landline side of the telecommunications world in the past decade are the advances in broadband (with all the new uses thereby made possible), not the sharing of old infrastructure. The advances in broadband have taken place in a vigorously competitive world – cable technology versus, first, DSL technology and, now, fiber optic and wireless technology.[2] The facilities-driven competition has been so vigorous that the FCC, in 2005 (after the period at issue in this case), concluded that market freedom by the incumbents was the proper substantive choice of how to exercise its regulatory authority over provision of DSL transport service to dependent

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[1] Rule 37 statement: All parties have consented to the filing of this brief. Petitioners' letter consenting to all amicus briefs is on file with the Clerk. Respondents' letter is being filed with this brief.

No counsel for a party has written this brief in whole or in part, and no person or entity other than the *amici curiae* or their counsel has made a monetary contribution to the preparation or submission of this brief.

[2] *See, e.g.*, FCC, Wireline Competition Bureau, Indus. Analysis & Tech. Div., *High-Speed Services for Internet Access* (Mar. 2008), at hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-280906A1.pdf.

DSL retail providers. *See Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205 (3d Cir. 2007) (upholding FCC's removal of common carrier regulations from telephone company broadband services), *aff'g*, *In re Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, 20 FCC Rcd 14,853 (2005).

Starting in the late 1990s, firms that did little if any investing in competitive facilities, but sought instead to piggyback on the old infrastructure, commenced costly antitrust litigation against Verizon and other incumbent telephone providers. That litigation, which asserted claims under Section 2 of the Sherman Act that the incumbents had to provide their upstream (wholesale) services and facilities to downstream (retail) rivals so as to enable the latter to compete, was a drain on Verizon and others seeking to focus on broadband progress. This Court in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004), rightly brought that litigation to an end, recognizing that the litigation powerfully undermined, rather than served, the goals of antitrust law. The Ninth Circuit, in conflict with four other circuits, has resurrected a means to create the harm that this Court had stopped in *Trinko*.

With respect to high-speed services like the one at issue here, following the Court's decision in *Trinko* and the FCC's decision to stop requiring telephone companies to share their broadband networks, Verizon has been investing vast sums to deploy a fiber optic network to consumers.[3] Verizon has a strong interest

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[3] Verizon is investing $23 billion to offer fiber optic connections to 18 million households by 2010. *See* Devona Walker, *Verizon builds fiber-optic battlefield*, Herald Tribune, Apr. 15, 2007; Verizon press release (June 18, 2008), investor.verizon.

in the development of sound antitrust principles, which should protect unilateral decision-making from the costs and risks of antitrust litigation unless a clear rule of conduct has been both formulated and justified based on analysis of its systemic effects. Such rules must also avoid both capping prices on services deriving from beneficial, risky investments and penalizing retail price reductions that benefit consumers by intensifying competition against rivals (like cable). For those reasons, Verizon urges this Court to reject categorically respondents' (linkLine's) Sherman Act § 2 "price squeeze" claim.

The National Association of Manufacturers is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. The NAM's mission is to enhance the competitiveness of manufacturers by shaping a legislative and regulatory environment conducive to U.S. economic growth and to increase understanding among policymakers, the media, and the general public about the vital role of manufacturing to America's economic future and living standards.

SUMMARY OF ARGUMENT

This Court should reverse the Ninth Circuit's decision allowing linkLine to proceed on its price squeeze claim. *First*, the specific result in *Trinko* precludes the claim. The Ninth Circuit accepted that, under

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com/news/view.aspx?NewsID=925 (Verizon's fiber-to-the-premises network currently reaches 10 million premises). Verizon is the first major telecom company to deploy gigabit passive optical network (G-PON) technology to customers in the United States, which dramatically increases Internet access speeds. Verizon press release (Mar. 27, 2007), *see* investor.verizon.com/news/view.aspx?NewsID=825.

Trinko, petitioners (AT&T) had no antitrust duty to deal with linkLine at all – no antitrust duty to sell the upstream service (DSL transport) to linkLine. Under that correct premise, linkLine cannot have a cognizable claim alleging a price squeeze, which asserts a duty to sell at a price that allows linkLine to compete. "A defendant that has no duty to deal with rivals by definition has no duty to deal with them on particular terms that would permit them to compete." U.S. Invitation Br. 10.

Second, even aside from what is implied by the result of *Trinko*, the analytic methodology of *Trinko* precludes linkLine's price squeeze claim. Here, as in *Trinko*, the claim asserted goes beyond anything this Court has ever recognized. Here, as in *Trinko* (and other precedents of this Court), the antitrust analysis required for adopting duties toward rivals that curtail unilateral firm decision-making – an analysis that at its core requires consideration of systemic effects and institutional suitability – argues compellingly against newly recognizing the claim. And here, as in *Trinko*, the case against newly recognizing linkLine's claim is confirmed by the fact that there already is a regulator, with considerably greater expertise and flexibility than judges and juries in antitrust cases, that can address any legitimate aspect of the rival's grievance.

ARGUMENT

I. The Result in *Trinko* Bars linkLine's Price Squeeze Claim

The Ninth Circuit accepted the district court's holding, which is not before this Court, that under this Court's decision in *Trinko* AT&T had no duty to deal with linkLine at all. Pet. App. 1a, 5a & n.6, 77a-85a.

That premise, moreover, is correct: it follows directly from *Trinko*'s explanation of the outer limits of any antitrust duty to deal. AT&T did not voluntarily sell DSL transport (which is different from the retail service of DSL access) to outsiders or bar linkLine from buying AT&T's retail service at retail prices. *See* Pet. Br. 20. Under *Trinko*, linkLine could not establish a duty to deal.

Without a duty to deal, linkLine cannot sustain a price squeeze claim. If AT&T may simply refuse DSL transport to linkLine, as far as Section 2 is concerned, there can be no Section 2 duty governing the price AT&T charges. The United States so explained at the petition stage, as already quoted. Page 4, *supra*. The leading treatise agrees: "it makes no sense to prohibit a predatory price squeeze [what linkLine claims here] in circumstances where the integrated monopolist is free to refuse to deal." IIIA P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 767c5, at 129-30 (2d ed. 2002).

Indeed, in *Trinko*, because it was undisputed and indisputable that dealing was in fact under way, the duty to deal asserted, and rejected, was a duty to deal on terms that would enable at least some rivals to compete in the retail market. Any lesser duty, moreover, would have been immaterial to antitrust policy. Yet linkLine makes the same claim, as it must in order to invoke *competition* benefits – a necessary precondition to any antitrust claim. The focus on prices specifically does not take linkLine's claim outside the scope of *Trinko*'s rejection of a duty to deal. *Trinko* is not limited to claims to better *non-price* terms; nor could it sensibly be so limited, for price and service terms are intimately related. *AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 223 (1998). *Trinko* thus

expressly noted that it was rejecting the claim to judicially determined prices for the service Trinko demanded. 540 U.S. at 408. *Trinko*'s result thus bars linkLine's claim.

II. Proper Section 2 Analysis, Reflected in the Reasoning of *Trinko* and Other Precedents of This Court, Bars linkLine's Price Squeeze Claim

Because substance must determine whether there is a Section 2 duty, by any name, it is important to explain directly why a proper Section 2 analysis bars linkLine's claim. That claim asserts that a monopolist has a duty not just to avoid predatory pricing but, further, to avoid some *relation* between its wholesale and retail prices – one that squeezes the retail rival that also buys the wholesale input. A proper Section 2 analysis, however, as reflected in *Trinko*'s reasoning and other decisions of this Court, should lead to a categorical rejection of this claim.

This Court's reasoning in *Trinko* contained three major components. *First*, this Court had never recognized a duty to deal as expansive as Trinko asserted (whether called a duty to deal or "essential facilities" or something else). 540 U.S. at 408-12. *Second*, fundamental antitrust policies, both substantive and institutional, would be undermined by recognizing the newly expanded asserted duty to deal. *Id.* at 407-08, 414-15 (stressing investment incentives, administrability, deterrence of desirable conduct, *e.g.*). *Third*, the availability of regulatory authority to address any valid concerns confirmed that new recognition of Trinko's claim was improper. *Id.* at 411-13. This logic precludes linkLine's claim as well.

A. This Court's Precedents Do Not Recognize a Price Squeeze Claim

In *Trinko*, this Court recognized that it had some precedents involving a duty to deal. It then explained why Trinko's claim fell outside those precedents. And it therefore recognized that, to permit Trinko's claim to go forward, it would have to recognize a Section 2 duty it had never before recognized. 540 U.S. at 408-12.

The conclusion that a new Section 2 duty is being sought follows even more directly here. This Court has never recognized a price squeeze claim at all. U.S. Invitation Br.10-11. Only a few appellate court decisions, not any decision of this Court, have recognized price squeeze claims. linkLine asks the Court to do so for the first time, and in the face of strong judicial, government, and scholarly criticism of the appellate price squeeze cases generally and outright rejection of price squeeze claims in the present setting by circuits outside the Ninth. *See* Pet. 11-14, 18-22.

The decision that undergirded the smattering of pre-*Trinko* price squeeze decisions in the circuits is the Second Circuit's decision, written by Judge Learned Hand, in *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) (*Alcoa*). But, even aside from whether linkLine's allegation of a monopolized downstream market fits under *Alcoa*'s reasoning (*but see* Economists' *Amicus* Pet. Br. 9), the core logic of *Alcoa* should not be approved by this Court. The essential premises of *Alcoa* were that (a) "exercise" of market power by itself is condemned by Section 2 (148 F.2d at 438) and (b) Section 2 protects small rivals as such, even "in spite of possible cost" to consumers (*id.* at 429). But *Trinko* confirms that the former premise is incorrect, as the "charging of monopoly prices[ ]

is not only not unlawful; it is an important element of the free-market system." 540 U.S. at 407. And, as the United States explained (U.S. Invitation Br. 13), the focus on protecting competitors has long since been rejected by this Court in favor of a systemic focus on consumer welfare as it is enhanced by the overall process of competition, which sometimes results in monopolies as firms vie, through innovation and low pricing and other means, to get all the sales they can. As Judge Posner wrote, in describing the outmoded character of the *Alcoa* premises, "now that the *Alcoa* doctrine is defunct, it is understood that a monopolist is free to compete." R. Posner, *Antitrust Law* 250 (2d ed. 2001).

B. The Analysis Required for Consideration of Section 2 Duties Applicable to Unilateral Conduct Requires Rejection of linkLine's Price Squeeze Claim

Harm to a competitor is not, in itself, a harm against which antitrust law protects. *See Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977) (antitrust law protects "*competition*, not *competitors*") (internal quotation marks omitted); *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.* 509 U.S. 209, 224 (1993). That is equally true when a monopolist's conduct is at issue. U.S. Invitation Br. 11. A firm has no antitrust duty to rein in its efforts to capture every available sale in order to protect the health or survival of competitors. Stifling of vigorous competitive and innovative efforts to best rivals, and encouraging pricing or margin-preserving accommodations that protect rivals, are anathema to antitrust policy. *See Trinko*, 540 U.S. at 408 ("the supreme evil of antitrust [is] collusion").

These fundamental principles recognize that the most legitimate kinds of competition – the kinds of conduct that antitrust law most wants to encourage, such as innovations that offer what rivals do not or prices lower than those of rivals – are harmful to rivals in fact and in intent. What is crucial, therefore, is distinguishing the types of conduct that should be condemned as improper from entirely proper conduct, where the effect and intent may be the very same. *Trinko*, 540 U.S. at 407. The conclusion of an analysis identifying when the line has been crossed is to say that the conduct is "anticompetitive," "exclusionary," or "predatory," but such terms better express the conclusion (indeed, can easily be misunderstood to cover legitimately anti-rival conduct) than the analysis needed to arrive there.

1. Clear Formulation and Affirmative Justification Based on Systemic Effects and Institutional Suitability Are Preconditions To Recognizing Any Section 2 Restriction on Unilateral Conduct

The conduct at issue here is classic unilateral firm conduct, which the Sherman Act treats differently from concerted action. In particular, an especially strong presumption against antitrust intervention applies to unilateral conduct, as distinguished from concerted action that takes the form of promises about how the parties will make future choices about what they buy or sell. *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 767-69 (1984); *see* Areeda & Hovenkamp, ¶ 772d, at 192-93; *Trinko*, 540 U.S. at 410 n.3 (distinguishing concerted from unilateral refusals to deal). The dichotomy reflects an elementary truth: unilateral action that harms rivals is inherent in competi-

tion, and so restricting it through antitrust law carries distinctive risks of harming competition itself. *Copperweld*, 467 U.S. at 767-68 (harm to rivals inherent in competition; unilateral conduct governed by standards that seek to "reduce[] the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur").

At least two related premises support the demand for special justification before antitrust law intervenes to restrict unilateral conduct. *First*, antitrust policy is disserved by rules of law that discourage any firm, including a monopolist, from adopting efficient practices and vigorously competing to the detriment of rivals. Consumers suffer from such self-restraint. Not only do they miss the direct benefits (*e.g.*, of lower prices enabled by the efficiencies), but they are harmed indirectly, as actual and potential rivals can afford to be lazy under the monopolist's "umbrella" – rivals need not do as much, whether through innovative leap-frogging or otherwise, to match or to improve upon the monopolist's offerings if the monopolist is "pulling its competitive punches." *Olympia Equip. Leasing Co. v. W. Union Tel. Co.*, 797 F.2d 370, 375 (7th Cir. 1986) (per Posner, J.)

Second, it is hard to distinguish legitimate rival-harming unilateral conduct from conduct that should be condemned through antitrust law. *See Trinko*, 540 U.S. at 408 (relying on "the difficulty of identifying and remedying anticompetitive conduct by a single firm"); *id.* at 414 ("[U]nder the best of circumstances, applying the requirements of § 2 'can be difficult' . . . ."); *Copperweld*, 467 U.S. at 767-68 ("it is sometimes difficult to distinguish robust competition from conduct with long-run anti-competitive effects"); *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 21 (1st

Cir. 1990) (per Breyer, C.J.) ("almost all business activity, desirable and undesirable alike, seeks to advance a firm's fortunes at the expense of its competitors"); *id.* at 23 ("Merely eliminating competitors is not necessarily anticompetitive, for, as we explained earlier, even legitimate business activity that succeeds in helping a firm will likely disadvantage the firm's competitors."); Evans & Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 73, 75 (2005) ("the welfare effects of unilateral practices are inherently difficult to assess").

For those reasons, Section 2 law must guard against multiple dangers in restricting unilateral conduct and, moreover, must do so by requiring formulation and justification in a rule assessed for its systemic effects. To begin with, Section 2 grounds for intervention must try to minimize case-specific social costs. Thus, they must seek to avert false positives (antitrust condemnation of conduct that should be allowed) – which "'are especially costly, because they chill the very conduct the antitrust laws are designed to protect.'" *Trinko*, 540 U.S. at 414 (quoting *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986)); *see id.* ("The cost of false positives counsels against an undue expansion of § 2 liability."). And the applicable antitrust rules must seek to keep the sheer costs of the antitrust litigation as low as possible. Case-specific error and administration costs are reason enough to demand clear screening mechanisms for meritless claims.

Lowering *systemic* costs is at least as important in framing sound standards for antitrust intervention. Antitrust doctrines have their principal effects in deterred conduct that never makes its way into litiga-

tion – yet whose very deterrence may be harmful to antitrust policy. And systemic costs are inherently dependent on the suitability for judges and juries of the tasks an asserted duty would impose on them. This kind of analysis must be central to sound Section 2 law, not an afterthought to an analysis driven by case-specific considerations.

A business's decision whether to adopt a legitimate, but rival-harming, practice will inevitably be influenced by its prediction of how likely it is that the practice will be erroneously condemned in antitrust litigation, which may well be initiated by the harmed rival or take the form of a customer class action, generating treble damages and attorneys' fees. Such decisions will also be influenced by the expected high costs of defending the practice. *See South Austin Coalition Community Council v. SBC Communications Inc.*, 191 F.3d 842, 845 (7th Cir. 1999) ("[a]ntitrust litigation can be very costly"); *Virgin Atlantic Airways Ltd. v. British Airways PLC*, 257 F.3d 256, 263 (2d Cir. 2001) ("Wasteful trials and prolonged litigation that 'may have a chilling effect on procompetitive market forces' should be avoided."). Not only substantively overbroad rules, but rules that are difficult, vague, or otherwise unpredictable in application, and rules that simply require costly litigation, will deter businesses from engaging in legitimate competition, Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1, 14-15 (1984), and encourage use of litigation as a tool to dampen vigorous rivalry.[4]

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[4] *See* Baumol & Ordover, *Use of Antitrust To Subvert Competition*, 28 J. L. & Econ. 247, 254 (1985) ("[O]bscurity and ambiguity are convenient tools for those enterprises on the prowl for opportunities to hobble competition. As we know, it is not always necessary to win cases in order to blunt a rival's

Any articulated basis for antitrust intervention, at least for unilateral conduct, cannot be justified without careful consideration of these real-world costs and a consequent effort to define workable threshold requirements that protect against such systemic chilling of investment and vigorous competition.

Serious attention to these considerations is essential in order to prevent antitrust doctrine from turning the Sherman Act into a weapon for undermining the very policies the Act is supposed to promote. This Court relied on just such considerations in carefully limiting the grounds of antitrust intervention in *Trinko*, 540 U.S. at 407-08. Then-Judge Breyer explained the centrality of similar considerations in two First Circuit opinions, one of which rejected a price squeeze claim in a regulatory context but elaborated on some reasons for skepticism about such claims generally.[6] Judge Easterbrook, for the Seventh Circuit,

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competitive weapons. Harassment by lawsuit or even the threat of harassment can be a marvelous stimulus to timidity on the part of competitors. The potential defendant who cannot judge in advance with any reasonable degree of certainty whether its behavior will afterward be deemed illegal is particularly vulnerable to guerrilla warfare and intimidation into the sort of gentlemanly competitive behavior that is the antithesis of true competition."); *id.* at 264 ("Mere accusation and trial subjects the defendant firm to enormous expenses and even greater ex ante risks of an expensive adverse decision, even if it transpires ex post on the basis of convincing evidence that it is completely innocent.").

[6] Judge Breyer explained that, "while technical economic discussion helps to inform the antitrust laws, those laws cannot precisely replicate the economists' (sometimes conflicting) views. For, unlike economics, law is an administrative system the effects of which depend upon the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients. Rules that seek to embody every

explained that the mere theoretical possibility of competitive harm is not enough to justify recognition of claims.[6] And a similar theme informs the Antitrust Modernization Commission's recommended approach

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economic complexity and qualification may well, through the vagaries of administration, prove counter-productive, undercutting the very economic ends they seek to serve." *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (1st Cir. 1983). He later elaborated that antitrust rules "must be clear enough for lawyers to explain them to clients," "administratively workable," and "designed with the knowledge that firms ultimately act, not in precise conformity with the literal language of complex rules, but in reaction to what they see as the likely outcome of court proceedings." *Town of Concord*, 915 F.2d at 22. *See also* D'Amato, *Legal Uncertainty*, 71 Cal. L. Rev. 1 (1983) (describing costs of legal uncertainty).

[6] In *Schor v. Abbott Labs.*, 457 F.3d 608 (7th Cir. 2006), Judge Easterbrook wrote: "We appreciate the potential reply that it is impossible to say that a given practice 'never' could injure consumers. A creative economist could imagine unusual combinations of costs, elasticities, and barriers to entry that would cause injury in the rare situation. [Citing articles]. But just as rules of *per se* illegality condemn practices that almost always injure consumers, so antitrust law applies rules of *per se* legality to practices that almost never injure consumers." *Id.* at 612-13. "Rules for predatory pricing are good examples," resting on the premise that "[s]ubjecting all low prices to litigation, and the inevitable risk of error in a search for the rare instances in which consumers could be made worse off in the long run by low prices today, would make it more risky for firms to reduce prices, and they would be less inclined to do so – to consumers' considerable detriment." *Id.* at 613. Citing the Evans & Padilla article on the proper analytic framework, Judge Easterbrook explained that an antitrust claim requiring "a search for the rare situation" where antitrust harm might exist should be rejected as "not worth the candle," at least when "[t]he search itself (and the risk of error in the judicial process) has much more chance of condemning a beneficial practice than of catching a detrimental one." *Id.*

to Section 2 standards, though in the less clearcut manner that characterizes such across-the-spectrum consensus reports. *See* Antitrust Modernization Comm'n, *Report and Recommendations*, at 88-92 (2007) (at 88, *e.g.*: "In general, standards for applying Section 2 of the Sherman Act's broad proscription against anticompetitive conduct should be clear and predictable in application, administrable, and designed to minimize overdeterrence and underdeterrence, both of which impair consumer welfare."), govinfo.library.unt.edu/amc/report_recommendation/chapter1.pdf.

Antitrust policy thus must demand that several steps be taken before a court accepts as sound any asserted ground of Section 2 condemnation of unilateral conduct. The ground of condemnation must be formulated to make apparent the bases for condemnation. Once so formulated, the rule must be assessed – based on the difficulty or ease of making the judgments required by the rule, and an empirical sense of the relative frequency of legitimate versus illegitimate uses of the practice at issue – to predict how many false positives such a rule directed to a particular practice are likely to generate, and how many false negatives. That assessment will, in turn, depend centrally on the likely costs of the processes for making the crucial distinctions required by the rule, the reliability and accuracy of the processes for making the distinctions, and as a result the systemic costs for private businesses that have to live with the rule. It is likewise critical to consider, as between courts and the marketplace, which is more likely to correct errors, and after how long, and at what cost (erroneous judicial condemnations have to be corrected by later changes in law, erroneous judicial vindications have to be corrected by market displace-

ment). *See* Evans & Padilla, at 80-88; Hylton & Salinger, *Tying Law and Policy: A Decision-Theoretic Approach*, 69 Antitrust L.J. 469, 498-502 (2001).

In the abstract, these inquiries can be challenging. Partly for that reason, minimizing the challenge in practice requires proper assignment of the burden of proof. For unilateral conduct, the default rule must be non-intervention where the burden of formulation and justification in systemic terms is not met. The alternative is worse.

This framework accords with the sensible presumption that "[t]he costs of false convictions in antitrust decisions involving unilateral practices are likely to be significantly larger than those of false acquittals." Evans & Padilla, at 83. Moreover, at least in general, the presumption of skepticism about antitrust intervention for unilateral conduct sensibly reflects a presumption that the marketplace is a better corrective mechanism than the courts (or Congress). Expunging antitrust decisions that unsoundly restrict competitive conduct takes considerable time and effort, whereas allowing a practice that builds or reinforces monopoly power, if that power is exploited, invites entry. *Id.; see* Easterbrook, at 15. Our economic system is built on the general judgment that the incentive for profit (by those developing innovations and otherwise seeking entry when markets are monopolized) is a powerful force for undoing monopoly, just as the presumptively protected opportunity to charge monopoly prices "is what attracts 'business acumen' in the first place." *Trinko*, 540 U.S. at 407.

These considerations apply in particular to any antitrust limitations on unilateral firm pricing decisions. *Brooke Group* adopted an objective and demanding set of necessary requirements for a claim that

prices are too low, because of the institutional limits of courts and the strong dangers of over-deterrence from any less demanding standard, even though some potentially bad conduct might therefore fall outside antitrust proscription. 509 U.S. at 223-26. More recently, *Weyerhaeuser* affirmed those principles and borrowed the predatory-pricing standard to set a comparably limiting standard for any claim of predatory purchasing. 127 S. Ct at 1076-77. Where unilateral pricing is at issue, the strong presumption must be that the strict standards for predatory pricing (or bidding) are the only standards.

2. Recognizing a Price Squeeze Claim Would Undermine Fundamental Antitrust Policy

A price squeeze theory of Section 2 liability should be rejected categorically because the potential competitive gain from recognizing a price squeeze inquiry is hard to identify even theoretically and at best slim, the separation of wheat from chaff is unreliable and costly, courts would have to take on an unsuitable role, and, worse, any price squeeze duty would present grave risks of deterring conduct *encouraged* by the antitrust laws. Even aside from the background role of regulation to catch any legitimate complaints, there is no substantial possibility of reliably identifiable harm that can justify the countervailing risks to desirable conduct and imposition on courts of inappropriate regulatory tasks that recognizing a price squeeze claim would entail. And a categorical rejection is required, because a murky or case-by-case approach, with uncertainty as to result and high costs of application, would produce many if not all of the same adverse substantive and institutional consequences as outright embracing of a price squeeze

theory. Accordingly, this Court should refuse to add to Section 2's recognition of a duty to avoid predatory pricing a new duty to avoid a combination of wholesale and retail prices that together produce a squeeze on retail rivals.

a. It is hard to identify even theoretically, let alone practically, what if any price squeezes are bad from the Section 2 perspective. A concern about harm to competitors *per se* is contrary to modern antitrust policy. Nor is "leveraging" of advantages derived from a monopoly from one level to another itself contrary to antitrust policy. Desirable conduct, such as exploiting efficiencies of vertical integration, can have that effect. Moreover, the effect itself may be beneficial even in the short run (if, *e.g.*, the result is to eliminate double marginalization that raises current prices), let alone in the longer term (by promoting innovative and other efforts to unseat a validly earned second monopoly). *See Town of Concord,* 915 F.2d at 24-25; Areeda & Hovenkamp ¶¶ 756b3 at 14-15, 767c2 at 128.

Leveraging of efficiencies that makes rivals' entry into the upstream business more difficult could not for that reason be condemned. Genuine efficiencies of vertical integration might make single-level entry more difficult, and scale resulting from efficiencies might make dual-level entry more difficult. Thus, even if the focus were on a particular alleged price squeeze, without yet turning to the necessary systemic-effects analysis, the result of making challenges to a wholesale monopoly more difficult is no reason for condemnation. In any event, there is no suggestion in this case that linkLine is a potential rival in supplying DSL transport (the wholesale product). Indeed, as this case illustrates, imposing

duties to protect retail rivals can easily harm investment and competition at the wholesale level (here, with rival providers of broadband transport).

Although *Trinko* confirms that there is nothing impermissible about seeking a monopoly profit, it is also the case that, in one ordinary situation, there is not even the genuine possibility of greater monopoly profits from acquiring a second monopoly. At least where the wholesale input and retail product are used in fixed proportions, as here, all the available monopoly profits can be earned simply by charging the monopoly price upstream. *Town of Concord*, 915 F.2d at 23; Pet. Br. 24. Even if AT&T had wholesale monopoly power, seeking greater monopoly profits cannot be the reason for pricing that effects a squeeze.

Moreover, price squeezes can result from conduct that is readily understood to be entirely innocuous, even positively desirable. *See* Areeda & Hovenkamp ¶ 767c, at 126-30. Market conditions, especially when multiple downstream products require an upstream input, can change the costs of or demand for the upstream product so as naturally to squeeze the margin of downstream rivals in at least some of the downstream products. ¶ 767c1, at 127. A price squeeze may result from price discrimination among different users of the upstream product, which can be output enhancing (allowing those who value the product less to obtain it when a uniform price might cut off such purchasers). ¶ 767c4, at 129. Most generally, perhaps, rival downstream firms may be less efficient than the defendant firm, whose very integration into both levels may be a source of greater efficiency. ¶ 767c3, at 128.

In short, there is no readily available, sound definition of what if any price squeezes should be con-

demned – even putting aside the uncertainties and difficulties of identifying them reliably in practice and the systemic effects of rules that allow for the search. But those aspects of a proper Section 2 analysis clinch the case against a price squeeze claim.

b. As *Brooke Group*, *Trinko*, and *Weyerhaeuser* all make clear, a central aspect of any Section 2 analysis is "the institutional fact that antitrust rules are court administered rules." *Town of Concord*, 915 F.2d at 22. Here, entertaining the price squeeze theory promoted by linkLine and the Ninth Circuit would entail complex and inherently uncertain inquiries. *Id.* at 25 ("it is not easy for courts to administer Judge Hand's [*Alcoa*] price squeeze test"). The sifting out of cases involving the innocuous explanations just noted is itself a difficult and uncertain enterprise, especially but not only in the absence of some positive formulation identifying which price squeezes were to be condemned. *See* pages 10-11, *supra*. And even a direct focus on prices presents intractable problems.

The essential basis for promoting recognition of a price squeeze claim – over and above the available predatory pricing claim – is the notion that the *relation between wholesale and retail prices* should allow room for efficient retail competition. Yet:

> Identifying the "appropriate" price is an extraordinarily complex regulatory exercise. Presumably, the tribunal would have to determine the amount that an efficient rival would require as a distribution between the defendant's wholesale price to the rival and its own downstream price to consumers. But this raises problems of a different order of magnitude than those encountered in a predatory pricing case. The tribunal would have to identify the markup required by a

> hypothetical "efficient" rival in a market with high fixed costs and numerous joint costs. Even then, it is difficult to see any consumer benefit in a rule that requires a firm to share its inputs with rivals so that they can sell together in the downstream market.

P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 787c, at 237 (Supp. 2008) (footnote, which cites economic literature on required complex inquiry, omitted).

The situation is particularly complex when multiple "products" are produced using shared inputs. This phenomenon is commonplace in the telecommunications industry, where multiple services (which may or may not be different antitrust "products") are provided using common network and switching facilities and common provisioning, billing, and other systems and personnel. linkLine's claim presents intractable problems in this context:

> Adjudicating this claim will require a court first to discern and second to guess how a firm allocates fixed costs through its pricing of diverse products that use the fixed-cost base. That task is well nigh impossible . . . . [T]here is no single correct way for a multi-product firm to allocate fixed costs through the pricing of its diverse products, and once a fixed-cost structure is in place any price above the incremental cost of serving a particular customer is "rational" in the sense that it contributes more to covering the fixed costs than not serving that customer at all.

Id. at 236.

And the problems are still worse given the prevalence of "bundling" throughout the economy – the offering of several "products" together at a single

price different from the sum of the prices of each "product" offered alone. In the telecommunications world, the efficiency reasons that drive bundling generally, including shared costs and transactional savings, have produced familiar bundles of services: *e.g.*, voice (landline or wireless); Internet access; video. In this common situation, there is uncertainty even about determining at the threshold what the effective prices of the defendant are, on a product-specific basis, let alone what they "should" be on some price squeeze theory.

These problems cannot be made to disappear by asking only whether the upstream price is actually lower than the defendant's downstream price. As a substantive matter, such a disparity cannot simply be condemned. The defendant's low retail price is lawful as long as it is not predatory under the demanding standards of *Brooke Group*; indeed, such a low price is an antitrust good even when rivals dependent on the defendant cannot compete as a result. (As a practical matter, the retail price can easily be driven down by retail competition that does not depend on the wholesale input from the defendant: *e.g.*, DSL Internet access competes directly with cable.) And this antitrust consequence does not change just because the defendant may also choose to use any upstream market power it may have to charge higher prices to outsiders for the input – as it is perfectly entitled to do. *See Trinko*, 540 U.S. at 407-08.

In any event, identifying a wholesale-higher-than-retail situation is not straightforward. The problems of identifying the relevant prices remain, and not just in the common situation of bundling, at either the wholesale or retail level. For example, offering DSL Internet access may produce multiple sources of

revenue: not just any retail price for access, but advertising fees paid by firms other than the access user (as is increasingly common on the Internet today). A focus on just one retail price would be unsound. More generally, in a fast-changing business, like telecommunications, a particular "retail service" may be an essential element of a strategy to compete in a marketplace moving toward bundled offerings (*e.g.*, voice or video revenues may be enhanced by offering Internet access, whose price therefore cannot be viewed in isolation).

c. The regulatory inquiries required by recognition of a price squeeze claim are plainly not suitable for decision by judges and juries in antitrust cases. Then-Judge Breyer, speaking for the First Circuit, explained how foreign to antitrust courts are the needed inquiries. *Town of Concord*, 915 F.2d at 25. And this Court in *Trinko* expressly endorsed the principle that such institutional unsuitability was an important reason to refuse to recognize a claimed Section 2 duty: when the tasks required cannot be reliably performed, any claim of harm – at least if otherwise uncertain – "should be deemed irremedia[ble] by antitrust law." *Trinko*, 540 U.S. at 415 (internal quotation marks omitted).

The price squeeze claim at issue here fits that description for multiple reasons. The inquiries that would be required are particularly technical, requiring an expertise – including continuing familiarity with the industry – that is difficult for generalist judges or juries, having only episodic involvement with the topic and generally lacking specialist training, to acquire within the time limits of cases, conducted through formal adversarial processes. Perhaps as important as the comparative expertise of

regulators is their flexibility. Even within regulatory agencies, price, cost, and competition inquiries are inherently uncertain, and therefore the determinations made are intrinsically experimental and subject to change when errors are discovered or circumstances change. That kind of flexibility as to substantive prescriptions, coupled with remedial flexibility, is not matched in antitrust cases. *See Trinko*, 540 U.S. at 415 (courts should impose no antitrust duty that "'requires the court to assume the day-to-day controls characteristic of a regulatory agency'"); *see* Antitrust Modernization Commission, *supra*, at 102 ("Moreover, forced sharing requires courts to determine the price at which such sharing must take place, thereby transforming antitrust courts into price regulators, a role to which they are ill-suited.") (footnote omitted).

d. As already noted, *Trinko*, *Brooke Group*, and *Weyerhaeuser* all confirm the essential need to avoid overkill in antitrust law, especially for unilateral conduct. In the present context, the harms from false positives – indeed, of the *risk* of false positives or, even the costs of litigating about the issue – are clear and severe. Most specifically, an error in an individual case produces case-specific harm of the most obvious type. If the tribunal judging prices makes "any error whatsoever, giving the rival a higher markup than necessary to insure minimum efficient operation, the impact of the ruling would be *higher* prices for consumers." Areeda & Hovenkamp ¶ 787, at 238.

More systemically, firms faced with the prospect of price squeeze liability or litigation have incentives to do one or more of four things: raise their downstream prices to protect their rival; lower their upstream prices; abandon selling to the downstream rival alto-

gether; or abandon their own downstream sales. The incentives are powerful, and the consequences are harmful. *See* Areeda & Hovenkamp ¶ 767d2, at 133 (criticing *Alcoa* approach as "confront[ing] a monopolist with two choices: to forgo monopoly profits or to avoid or abandon partial vertical integration. It is thus inconsistent with either of two other basic legal propositions: that a lawful monopolist is entitled to charge a monopoly price, and that partial vertical integration by a monopolist is presumptively lawful because it is economically beneficial.").

Raising the downstream price works perhaps the most direct harm in antitrust terms. This Court has based its strict preconditions for predatory pricing on the value placed on low end-user prices. *Brooke Group*, 509 U.S. at 224; *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990); *see Weyerhaeuser*, 127 S. Ct. at 1074 ("We were particularly wary [in *Brooke Group*] of allowing recovery for above-cost price cutting because allowing such claims could, perversely, 'chill legitimate price cutting,' which directly benefits consumers."); *see also Town of Concord*, 915 F.2d at 27.[7] And the adverse effects of raising downstream prices extend beyond the immediate harm to consumers: the downstream rivals

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[7] *See* Thomas O. Barnett, Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Opening Remarks at the Antitrust Division and FTC Hearings Regarding Section 2 of the Sherman Act: The Gales of Creative Destruction: The Need for Clear and Objective Standards for Enforcing Section 2 of the Sherman Act (June 20, 2006) ("In *Brooke Group*, the Court recognized the possibility that above-cost pricing might hurt competition but nonetheless insulated above-cost pricing from liability to avoid the greater harm of a legal regime that would cause firms to hesitate before lowering their prices or not to lower prices at all.") (footnote omitted).

themselves face diminished incentives to find better ways to compete when an umbrella is held over their heads to protect them.

Lowering the upstream price, for fear of litigation costs or liability, is an antitrust harm as well. The compelled curtailment of monopoly prices is not just outside what Section 2 requires. As *Trinko* explains, it undermines Section 2's policy, because the prospect of above-cost prices is an important driver of risky investments and innovation on which the competitive system overall depends. 540 U.S. at 407-08.[8] Recognizing linkLine's price squeeze claim would impair incentives to invest, both by putative monopolists (the reward would be less) and by rival firms (there will be less need).

The price squeeze scenario requires partial vertical integration, and that structure can be avoided in either of two ways. As far as antitrust law is concerned, the defendant may simply stop selling to the plaintiff rival – in the absence, as here, of a Section 2 duty to deal. Among other problems, the rival cannot possibly have standing to encourage that consequence, for the rival's claim of price squeeze depends on the assertion that it positively needs to buy from the defendant. Alternatively, the defendant can remove itself from the downstream market.

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[8] *See* Thomas O. Barnett, Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Presented at the Fordham Competition Law Institute, 34th Annual Conference on International Antitrust Law & Policy: Section 2 Remedies: A Necessary Challenge (Sept. 28, 2007) (prescribing the "advice of Hippocrates" for Section 2 – "help, or at least . . . do no harm" and noting that "imposing a duty on a defendant to provide competitors access to its assets . . . can undermine the incentive of those other competitors to develop their own assets as well as undermine the incentive for the defendant competitor to develop the assets in the first instance").

Both results – or movements in either direction – are generally harmful. Partial vertical integration is, quite broadly, "economically beneficial." Areeda & Hovenkamp ¶ 767d2, at 133. Indeed, as Judge Posner noted long ago, partial vertical integration – both supplying and competing against a firm – is commonplace in our economy. *General Leaseways, Inc. v. Nat'l Truck Leasing Ass'n*, 744 F.2d 588, 593 (7th Cir. 1984). The prevalence of a practice among competitive firms powerfully indicates efficiency, because competition from rivals otherwise would force abandonment of the practice. *See* Evans & Padilla, at 81 ("Consider a practice in which firms in both competitive and uncompetitive markets engage. We would expect that the practice cuts costs or enhances value to customers – after all, competitive firms cannot survive indefinitely if they do not use the most efficient methods of producing, designing, and distributing products."); Hylton & Salinger, at 497-98. That conclusion applies when a monopolist engages in the practice as well: "There is no economic reason to believe that these efficiencies become less important as firms acquire market power." Evans & Padilla, at 81; *id.* at 91 (the "sources of efficiency remain, regardless of the degree of market power of the firm engaging in the practice"). It is therefore harmful to proscribe or deter such conduct on the part of firms with market power, which also have an incentive to pass on at least some of the benefits of efficiencies to their customers. Hylton & Salinger, at 504. Judge Posner summarized the point:

> If the practice is one employed widely in industries that resemble the monopolist's but are competitive, there should be a presumption that the monopolist is entitled to use it as well. For its widespread use implies that it has significant

> economizing properties, which implies in turn that to forbid the monopolist to use it will drive up his costs and so his optimum monopoly price.

R. Posner, *supra*, at 253; *see* Epstein, *Monopoly Dominance or Level Playing Field? The New Antitrust Paradox*, 72 U. Chi. L. Rev. 49, 60 (2005).

Deterring partial vertical integration would undermine this efficiency-enhancing practice. Rivals may be more efficient at certain downstream functions than the defendant, so that an incentive to refuse to deal altogether would be harmful not just to the rival but to overall competition. By the same token, the defendant may be more efficient in the downstream market than rivals, so that an incentive to withdraw from that market would remove both an efficient competitor and a spur to other firms in that market to improve their own performance.

All of these are grave risks presented by anything less than a categorical rejection of price squeeze claims as unjustified. As already explained, unilateral firm conduct is driven by an assessment of the high costs and risks of antitrust adjudication. Firms will avoid conduct that can trigger the launching of litigation, which can drain treasuries and be profoundly distracting to officers and employees that must remain focused on the business. They will even more readily be driven to damaging conduct-avoidance behavior by the inherent uncertainty of the outcome of price squeeze litigation. The complexity of the inquiries demanded means that there is an ineradicably high risk in seeing litigation to its conclusion, no matter how seemingly clear the lack of merit in the claim.

It is not a sound answer that an ability to exercise market power in the sale of the upstream product is a prerequisite. The foregoing analysis of harmful deterrence squarely applies to firms with market power. In any event, firms without market power would be harmed as well. Market definition and power, in practice, are often not decided (even on summary judgment) until the parties have incurred considerable costs for discovery and expert analysis directed to potentially complex facts about market structure and firm behavior. The burden of a price squeeze rule will therefore be felt by successful firms that ultimately would not be held to have market power – as should be apparent in the context of broadband services, where the strength (often the lead) of cable companies must ultimately preclude a claim that the local telephone companies have market power here.

C. Expanding Section 2 To Recognize Price Squeeze Claims Is Especially Inadvisable in the Presence of Regulatory Authority Over the Conduct

All of the foregoing provides compelling reasons to reject a price squeeze claim. This Court recognized in *Trinko*, moreover, that a final reason for rejecting a Section 2 duty is present when regulatory authority in fact exists to address any legitimate aspects of the grievance asserted. That conclusive reason against expanding Section 2 duties is present in this case as well.

During the period at issue in this case, AT&T's wholesale DSL prices (for its transport service) were actually subjected to FCC common-carrier regulation under an approach that forced incumbent telephone

companies, if they provided DSL-based Internet access (retail) services to end-users, to offer the incorporated transport on a nondiscriminatory common- carrier basis to rival providers of the end-user retail access service. *See* Pet. 4 n.1. Subsequently, this Court concluded that the statute, as amended in the 1996 Telecommunications Act, provided room for discretion about the separation of an underlying transport component from the end-user access service. *National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967 (2005). Exercising the authority thus recognized, the FCC then made a substantive determination that competition and related policies would be promoted by *not* compelling this wholesale common-carrier offering. *See Time Warner Telecom*, 507 F.3d at 214, 220-23.

The FCC has thus exercised its regulatory authority to determine what forms of substantive regulation, if any, should apply to the upstream input at issue here. That authority readily encompassed consideration of the competition issues on which linkLine premises its Section 2 claim. Indeed, in another context (approval of an application for permission to enter the long distance business under 47 U.S.C. § 271), the D.C. Circuit required the FCC to address these very considerations under its Section 271 mandate, *Sprint v. FCC*, 274 F.3d 549, 554-55 (D.C. Cir. 2001), and the FCC did so, *see, e.g.*, *Order on Remand*, 18 FCC Rcd 24,474 (2003); *Order on Remand*, 19 FCC Rcd 2839 (2004).

This regulatory backdrop cements the reasons this Court should not recognize a price squeeze claim for the first time. Even without regulation at the retail level, regulatory authority at the upstream-input level can readily address any true competition issues:

among other things, the upstream-input price can be analyzed in light of the retail price (what it actually is or what it may be), even if the latter is not directly controlled. And, as already explained, regulators are plainly better positioned than judges or juries in antitrust cases to make the inherently uncertain, experimental, and transitory determinations about pricing, and the effects on investment and innovation, that are necessary components of a price squeeze analysis.

The FCC's 2005 deregulation of wholesale DSL service does not change the conclusion. The FCC concluded that, with the reality and importance of broadband rivalry between the telephone and cable companies, the best policy for competition is freedom as to the upstream input. That was an exercise, not an abdication, of the FCC's regulatory authority. And the substance of that determination is diametrically opposed to linkLine's price squeeze claim.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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Supreme Court of the United States

PACIFIC BELL TELEPHONE COMPANY,
D/B/A AT&T CALIFORNIA, ET AL.
Petitioners,

v.

LINKLINE COMMUNICATIONS, INC., ET AL.,
Respondents.

On Writ of Certiorari to the
United States Court of Appeals
For the Ninth Circuit

BRIEF OF THE WASHINGTON LEGAL FOUNDATION AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether a vertically integrated alleged monopolist, with no antitrust duty to deal with its rivals, engaged in an unlawful "price squeeze" under federal antitrust law by leaving an insufficient margin between the wholesale price it charges its rivals and the retail price it charges consumers.

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INTEREST OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a public interest law and policy center based in Washington, DC, with supporters nationwide.[1] WLF engages in litigation and administrative proceedings in a variety of areas, and devotes a substantial portion of its resources to defending free enterprise, individual rights, and a limited and accountable government. To that end, WLF has frequently appeared as *amicus* in this and other federal courts to address the proper scope of the antitrust laws. *See, e.g.*, *Weyerhaeuser Company v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069 (2007); *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) ("*Trinko*"); *United States Tobacco Co. v. Conwood Co.*, *cert. denied*, 537 U.S. 1148 (2003); *In re Stock Exchs. Options Trading Antitrust Litig.*, 317 F.3d 134 (2d Cir. 2003).

WLF is concerned that the decision below expands antitrust liability beyond this Court's precedents, chills lawful, procompetitive conduct, and creates uncertainty in the law.

SUMMARY OF ARGUMENT

The Ninth Circuit's decision stands in stark contrast with this Court's recent antitrust decisions that have announced sensible and objective standards for the evaluation of unilateral pricing conduct under the antitrust laws. This Court's prior decisions allow

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[1] This brief is filed with the written consent of all parties, whose letters of consent are already on file with the Court. Pursuant to Rule 37.6, no counsel for either party authored this brief in whole or in part, nor did any party make a monetary contribution to the preparation or submission of this brief.

businesses to readily conform their conduct to the requirements of the antitrust laws and avoid unexpected antitrust exposure while competing aggressively and efficiently in the nation's markets. The Ninth Circuit's decision disrupts this settled landscape by applying different rules to firms that have vertically integrated, and thus undermines this Court's decisions in both *Trinko* and *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993).

The "price squeeze" claim recognized by the court below not only confounds established precedent, but also frustrates the animating purpose of the antitrust laws – to enhance competition. In short, the Ninth Circuit's holding will significantly chill legitimate, procompetitive conduct by imposing liability based upon facts that are unknown and unknowable to a business when it decides to set prices at the wholesale and retail levels. Such expansive and ill-defined liability rules burden commerce and chill robust economic activity. The resulting uncertainty will create a broad chilling effect on legitimate conduct, distorting the market, artificially skewing pricing decisions based on liability fears rather than sound economics, and thus harming consumers.

Expansive and ill-defined liability rules burden commerce and chill robust economic activity. *See, e.g.*, Steve Hantler, Washington Legal Foundation, *Judges Must Play Key Role In Stemming Tide of Asbestos Litigation* (May 7, 2003), *available at* http://www.wlf.org/upload/050903LBHantler.pdf; Victor E. Schwartz and Leah Lorber, Washington Legal Foundation, *Vaccine Liability Law Clarification Protects Lives and Resources* (January 6, 2003), *available at* http://www.wlf.org/upload/ 010603LBSchwartz.pdf.

The Ninth Circuit's decision imposes just such an imprudent burden on legitimate, procompetitive conduct, and should be reversed.

ARGUMENT

The Ninth Circuit's "Price Squeeze" Claim Defies Precedent, Antitrust Policy, And Market Reality

This case concerns the pricing decisions of vertically integrated businesses. A vertically integrated business may sell products or services to third parties at the wholesale level, while continuing to compete with those third parties at the downstream retail level. Petitioners here are vertically integrated with respect to Internet-access service – selling components of the service at the wholesale level to Respondents, and also competing at the downstream level for retail consumers purchasing Internet service.[2] Pet. App. 3a. Respondents have alleged that Petitioners have engaged in a "price squeeze" by leaving an insufficient margin between the price at which they sell inputs to Respondents at the wholesale level and the price at which they sell to consumers at the retail level to permit Respondents to compete.

The Ninth Circuit held that such allegations state a claim under the federal antitrust laws. Pet. App. 18a-19a. But recognition of a "price squeeze" claim is contrary to Supreme Court precedent, logic, and marketplace realities and, accordingly, should be reversed.

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[2] For purposes of this brief, WLF assumes the facts as set out by the Ninth Circuit to be correct.

A. The Ninth Circuit's Decision Renders Unlawful Conduct That This Court Has Held Is Lawful

In the decision below, the Ninth Circuit held that "[b]ecause a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*, those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko*." Pet. App. 14a. The Ninth Circuit's recognition of a "price squeeze" claim is inconsistent with this Court's precedents and the Court should reject it.

A "price squeeze" claim involves a vertically integrated firm that sells products or services to rivals at the upstream wholesale level while also competing with those rivals at the downstream retail level. *See, e.g.*, Julian O. von Kalinowski, 2 *Antitrust Laws and Trade Regulation* § 27.04[1], at 27-40 (2d ed. Matthew Bender 2007) (quoted in decision below, Pet. App. 8a). In this case, at the upstream level, where Petitioners are alleged to enjoy a monopoly position, Petitioners are alleged to have charged an excessively high price to Respondents. Pet. App. 5a-6a. At the downstream level, where Petitioners face competition from Respondents, they are alleged to have charged an excessively low price. The resulting "squeeze" allegedly deprives Respondents of the opportunity to earn a sufficient margin to compete. *Id.*

This Court's decisions establish the lawfulness of petitioners' pricing conduct under the antitrust laws. First, at the upstream level, petitioners are under no antitrust duty to deal with respondents under *any* terms, and so their unilateral setting of the price terms on which they are willing to deal is protected from antitrust scrutiny by the Court's decision in

Trinko, 540 U.S. at 410 ("We conclude that Verizon's alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim under this Court's existing refusal-to-deal precedents."). Indeed, "'it makes no sense to prohibit a predatory price squeeze in circumstances where the integrated monopolist is free to refuse to deal.'" *Covad Commc'ns Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 673 (D.C. Cir. 2005) (*quoting* 3A Phillip E. Areeda & Herbert Hovenkamp ("Areeda & Hovenkamp"), *Antitrust Law* ¶ 767c3 (2d ed. 2002)).

Second, at the downstream level, Petitioners' decision to charge lower prices fully comports with the antitrust law, in the absence of any allegation of predatory pricing. Thus, to render Petitioners' pricing decisions unlawful, Respondents must allege that the prices fall "below an appropriate measure" of their costs, *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222 (1993), and that they had "a dangerous probability of recouping [their] investment in below-cost prices," *id.* at 224. The Ninth Circuit's decision, however, would impose liability even in the absence of such predatory pricing allegations. Pet. App. 23a.

The Ninth Circuit's decision would thus circumvent established proof obligations under the antitrust laws. But this Court adopted its bright-line rules in *Trinko* and *Brooke Group* to promote certainty and administrability for businesses on both upstream and downstream pricing. At the upstream level, *Trinko* makes clear to businesses that, except in very narrow circumstances, it does not have an antitrust duty to provide assistance to its rivals. At the downstream level, *Brooke Group* assures businesses that, without

more, above-cost pricing will not support a predatory pricing claim. Under the Ninth Circuit's decision, both of these stable and certain rules would evaporate for a vertically integrated firm, which would now face liability under a theory that two rights make a wrong.

Furthermore, the Ninth Circuit's rule would punish businesses for becoming vertically integrated – conduct which, at least until now, has often been considered to be beneficial to consumers, *see, e.g.*, 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 757 (explaining how vertical integration can produce "significant cost reductions" by enabling production and transactional efficiencies). The decision below thus substantially unravels this Court's holdings in both *Trinko* and *Brooke Group*, and the stability in the law that they sought to establish, while expanding antitrust liability well beyond this Court's precedents.

B. The Ninth Circuit's "Price Squeeze" Frustrates Antitrust Policy

1. The Threat of "Price Squeeze" Liability Will Reduce Procompetitive Conduct

In straying from this Court's precedents, the Ninth Circuit's decision promotes unsound antitrust policy that will chill legitimate, procompetitive conduct and harm consumers.

This Court has long recognized the danger that expansive and ill-defined antitrust liability will chill benign and procompetitive conduct. *See, e.g.*, *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1964 (2007) (refusing to permit a Sherman Act § 1 complaint to proceed which alleged conduct "consistent with conspiracy, but just as much in line with a wide swath of ra-

tional and competitive business strategy unilaterally prompted by common perceptions of the market"); *Weyerhaeuser*, 127 S. Ct. at 1078 ("Given the multitude of procompetitive ends served by higher bidding for inputs, the risk of chilling procompetitive behavior with too lax a liability standard is as serious here as it was in *Brooke Group*."); *Trinko*, 540 U.S. at 414 ("Mistaken inferences and the resulting false condemnations 'are especially costly, because they chill the very conduct the antitrust laws are designed to protect.' The cost of false positives counsels against an undue expansion of § 2 liability." (internal citation omitted)); *Brooke Group*, 509 U.S. at 223, 224 (decrying the "intolerable risks of chilling legitimate price-cutting" and stating that "discouraging a price cut and forcing firms to maintain supracompetitive prices, thus depriving consumers of the benefits of lower prices in the interim, does not constitute sound antitrust policy").

The result of the Ninth Circuit's approach will be a broad chilling effect that will distort the free operation of the market at two levels. At the upstream level, even for firms that have an entirely lawful monopoly, antitrust liability would prevent mere unilateral price-setting, which the Court has recognized as "an important element of the free-market system" that "induces risk taking that produces innovation and economic growth." *Trinko*, 540 U.S. at 407.

At the downstream level, the risks from imposing antitrust liability on prices that are allegedly too low, but are above an appropriate measure of the seller's costs, are manifest, and have been acknowledged repeatedly by the Court. *See, e.g.*, *Weyerhaeuser*, 127 S. Ct. at 1074 ("We were particularly wary of allowing

recovery for above-cost price cutting because allowing such claims could, perversely, 'chil[l] legitimate price cutting,' which directly benefits consumers." (quoting *Brooke Group*, 509 U.S. at 223-24)); *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990) ("Low prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition."). Perversely, the more efficient a vertically integrated firm becomes, and the more it is able to lower prices to consumers, the more it exposes itself to potential antitrust liability under the Ninth Circuit's decision. That stands antitrust policy on its head.

2. The Ninth Circuit's Rule Is Inadministrable

The chilling effect of an unsound antitrust rule stems not only from the risk of a "false positive" finding of liability where none is warranted (although that risk is considerable), but also from the risk of expending considerable time, money, and distraction on the litigation process itself, as unclear and inadministrable liability rules encourage those who lose in the economic marketplace to shift their battle to the courtroom. As this Court acknowledged in *Twombly*, the risks and costs involved just in defending against private antitrust claims that ultimately prove to be baseless can be considerable.

> [I]t is one thing to be cautious before dismissing an antitrust complaint in advance of discovery, but quite another to forget that proceeding to antitrust discovery can be expensive. . . . It is no answer to say that a claim just shy of a plausible entitlement to relief can, if groundless, be weeded out early in the discov-

> ery process through 'careful case management,' given the common lament that the success of judicial supervision in checking discovery abuse has been on the modest side."

Twombly, 127 S. Ct. at 1967 (internal citations omitted).

What is more, the chilling effect of the Ninth Circuit's liability rule is more acute than in *Twombly* because there are few, if any, objective standards that would allow a vertically-integrated firm to determine prospectively whether it might commit a "price squeeze." The rule against horizontal price fixing at issue in *Twombly* is well-established and firms have experience in identifying and avoiding conduct that could result in a price-fixing claim.

Navigating the Ninth Circuit's judicially crafted pricing constraints, however, will be far more hazardous, if not impossible. According to the Ninth Circuit the firm must make sure that its upstream prices are not "so high," Pet. App. 8a, that its competitor/customers cannot compete downstream. This rule would require the firm not only to consider its own profit-maximizing price (as might any firm), but also to account for the multiple variables that determine whether its rivals will operate at a profitable level. In essence, the rule recognized by the Ninth Circuit would require a vertically integrated firm to take into account such factors as the cost structure and margin requirements of its downstream rivals when setting its own prices. One leading economic scholar has captured the difficulty of this approach as follows:

> Figuring out which way the results go is hard, because necessary data are almost always un-

> available or uncertain. *Moreover, the inquiry as to whether a price squeeze leads to competitive harm necessarily must be conducted ex post, which therefore makes it impossible for a firm to know in advance whether its pricing practices will be anticompetitive.*

Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct?*, 4(2) J. of Competition L. & Econ. 271, 276 (2008) (emphasis added); *cf. Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883, 905 (9th Cir. 2008) ("A potential defendant who is considering offering a bundled discount will likely not have access to information about its competitors' costs, thus making it hard for that potential discounter . . . to determine whether the discount it wishes to offer complies with the antitrust laws."). In short, under the Ninth Circuit's decision below, it will be virtually impossible for a firm to correctly ascertain in advance whether it is setting its upstream prices at a level that its rival will find acceptable, or whether its prices to consumers are too low to allow less efficient firms to compete.

The inadequacy of Rule 12(b)(6) as a screen against untenable price squeeze claims additionally gives such claims a greater chilling effect than the horizontal claims at issue in *Twombly*. *Twombly's* plausibility inquiry focused on whether the facts pled in the complaint sufficed to give rise to an inference of conspiracy, and Rule 12(b)(6) serves well to screen out claims where the underlying facts as pled are inadequate to support the conspiracy.

The allegations of a price squeeze pose a greater challenge to the courts. Allegations of prices "so high" for the input product that the rivals cannot compete

downstream do not readily lend themselves to dismissal because no inferences are necessary; instead these allegations would seem to require extensive factual development into the competitiveness of rivals. As the Court recognized in *Trinko*, however, the task of determining the "reasonableness" of a firm's prices is inappropriate for an antitrust court. "Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill suited." *Trinko*, 540 U.S. at 408. The Court made a similar point in *Brooke Group*, stating:

> As a general rule, the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, *or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting*.

Brooke Group, 509 U.S. at 223 (emphasis added).

The First Circuit has applied the same observation to a price-squeeze case, recognizing that a court cannot determine a "fair price" without "acting like a rate-setting regulatory agency." *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (Breyer, C.J.). The court acknowledged the difficulty in determining a reasonable price, identifying inefficient firms, and dealing with changes in a dynamic market. *Id.* It concluded that "we have said enough to show why antitrust courts normally avoid direct price administration, relying on rules and remedies (such as structural remedies, *e.g.*, prohibiting certain vertical mergers) that are easier to administer." *Id.*

Accordingly, unlike *Twombly*, where the federal courts may at least mitigate the risk from untenable claims, the federal courts are less able to screen out untenable price squeeze claims.

A further aggravating factor is that the price squeeze claim, while as matter of technical antitrust doctrine applies only to a monopolist, is not so easily confined in terms of its practical effect. It can be very difficult for a court to determine whether a particular firm has monopoly power, to say nothing of a lay person running a business. A firm would have to identify accurately the correct relevant market within which to measure its market share, correctly determine whether its market share was high enough for it to be considered a monopolist, and evaluate a host of other market factors, any one of which could change the outcome. *See, e.g., United States v. Dentsply Int'l, Inc.*, 399 F.3d 181, 187 (3d Cir. 2005) ("Other germane factors [in identifying a monopolist] include the size and strength of competing firms, freedom of entry, pricing trends and practices in the industry, ability of consumers to substitute comparable goods, and consumer demand."). Such determinations would be beyond the abilities of most businesses without incurring the expense of retaining counsel and an economist versed in antitrust economics. Given the practical difficulty of making the threshold determination of monopoly power, the risk of a broad chilling effect is even greater, potentially causing firms that may not meet the legal definition of a monopolist to nonetheless shy away from legitimate activity for fear of liability.

3. A Rule That Expands Antitrust Liability Should Not Uniquely Penalize Those Who Engage In Inherently Efficient Conduct

A price squeeze claim may well lead to some truly ironic situations where liability is imposed in circumstances simply contrary to sound antitrust policy. Consider a business with significant market share but below that which might plausibly give rise to a charge that it is a monopolist. Vertical integration into downstream markets could generate substantial efficiencies, lowering its costs and allowing it to achieve a competitive advantage over its rivals. If the firm has excess capacity at the upstream level, however, it might rationally continue to supply rivals. Through its "superior skill, foresight and industry," *i.e.*, the increased efficiency from vertical integration, it should capture more of the market and grow its share. *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945).

All of that would seem to be good and healthy competition under the antitrust laws. The catch comes, however, if the firm is so successful that it captures sufficient share to render it a monopolist. At that point, the rational firm might choose not to exploit the efficiency from its vertical integration for fear of the antitrust laws. The price squeeze claim thus runs headlong into the long-recognized principle of antitrust doctrine that "[t]he successful competitor, having been urged to compete, must not be turned upon when he wins." *Id.*

This hypothetical illustrates a general and likely sweeping effect of recognizing price squeeze liability: it will cause well-counseled firms to steer clear of con-

duct that could potentially impose legal liability, regardless of the economic efficiency and enhanced competition that the conduct would produce. Rather than face a lawsuit, a vertically-integrated firm may set prices at a level at which even its most inefficient rival would not be offended – a decidedly undesirable result for consumers. The consequences, as discussed by one scholar, are contrary to the goals of sound antitrust policy:

> Indeed, if the price of supplying a rival is a cessation of vigorous price competition with a rival, . . . so as to preserve profit margins of those participants who depend on rivals as a source of supply, then there may be an outbreak of peaceful price stability in the industry resulting from a chilling effect on price reduction. That result would harm consumers.

J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4(2) J. of Competition L. & Econ. 279, 294 (2008). Furthermore, some businesses may choose to avoid the risk of illegality by refusing to deal with rivals at all, or forsaking beneficial vertical integration that leads to increased efficiency and lower prices for consumers. However manifested, firms would be pricing their products and deciding to whom they sell them based on the fear of potential antitrust liability, not on the economically rational, and presumably efficient, prices that the market would dictate.

The uncertainty created by the decision below, and the resulting chilling effect on beneficial conduct, undermines the rule of law, and is directly at odds with this Court's repeated admonitions that antitrust liability should be no broader than necessary, so as not

to harm inadvertently the consumers the antitrust laws were designed to protect.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed.

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